No. 10,473

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

BYRON JACKSON CO., a corporation,

Appellant,

vs.

PATTERSON-BALLAGH CORPORATION, a corporation, J. C. BALLAGH and D. G. MILLER,

Appellees.

APPELLEES' BRIEF.

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APPELLEES' BRIEF.

Supplementary Statement of Facts.

Respondents concur generally in the accuracy of appellants' "Concise Statement of the Case" down to the second paragraph on page 4 of its brief. There it is stated that, shortly after defendant Miller acquired the shares of Patterson, the Board of Directors "was revamped in a manner dictated by Ballagh and Miller and thereafter consisted of Ballagh, Miller, one Howard Burrell * * *, one H. C. Armington * * * and E. S. Dulin, plaintiff's president." There is a footnote (App. Br. p. 5), "Dulin could not be dislodged; there was cumulative voting."

The real facts are that on August 4, 1938, long before Mr. Miller became a stockholder or connected with the Company, the Board of Directors of the corporation was increased from three to five members [R. 165-167], and, following this amendment of the by-laws, Messrs. J. C. Rennie and H. W. Elloitt were elected as the two additional members of the Board, the three then members being defendant J. C. Ballagh, C. L. Patterson and E. S. Dulin, plaintiff's president, *all of whom were present and voting.* The elections of Messrs. Rennie and Elliott were unanimous, *Dulin voting therefor* [R. 168]. The election of directors for the year 1939 occurred at the annual stockholders' meeting on January 27, 1939, at which time the five previous directors, to wit, Messrs. Patterson, Ballagh, Elliott, Rennie and Dulin were re-elected, *Mr. Dulin and plaintiff corporation both participating in the vote* [R. 198].

Defendant Miller did not acquire Patterson's stock nor succeed him as a director and officer until some time in February, 1939 [R. 211]. Director Rennie resigned at a special meeting of the Board on February 10, 1939 [R. 209] and defendant Miller was *unanimously* elected in his place. *Director Dulin seconded defendant Miller's nomination and voted for his election* [R. 211]. At this same meeting Patterson resigned as president and as a director and defendant Miller was nominated and *unanimously* elected president, *Director Dulin seconding his nomination and voting for his election* [R. 212]. At the same meeting H. C. Armington was nominated and elected a director in the place of Patterson, resigned, *Director Dulin seconding Armington's nomination and voting for his election* [R. 213]. At a special meeting of the Board on June 27, 1939, Director Elliott resigned [R. 220] whereupon Howard Burrell was elected in his place, *Director Dulin, the president and "representative*

of plaintiff," as he asserts, both seconding Burrell's nomination and voting for his election [R. 221].

This is the record notwithstanding the attempt in the language quoted from pages 4 and 5 of appellant's brief, to represent that the selection of directors Armington and Burrell was "dictated by Ballagh and Miller." Every step in the change of the personnel of the Board, which took place over a considerable period of time, was prominently participated in by plaintiff's president and representative Dulin and, of course, approved by him.

The footnote on page 5 of appellant's brief is equally misleading. There was never at any time any thought, suggestion or intimation of a desire on the part of defendants, or anybody else, to "dislodge" Dulin as a director and we suggest that this footnote is injected gratuitously as a further effort to misrepresent the situation. The facts are, and the record so shows, that the directors, including the defendants, were at all times solicitous of Dulin's prerogatives as a director and deferential to him in a high degree. For example, at a meeting of the Board of Directors on December 20, 1938, when matters of some importance were under consideration, the following entry appears in the minutes:

> "Mr. Ballagh then stated that when this matter was discussed at a previous meeting, Mr. Dulin had expressed the wish to have the matter of Mr. Rennie's employment held over until a later meeting to allow him time to study it over. Mr. Ballagh further stated that, inasmuch as Mr. Dulin was not present to vote, he preferred to not vote on the question." [R. 196.]

Upon a divided vote held during a directors' meeting on January 27, 1939, both Messrs. Patterson and Rennie voted with Mr. Dulin [R. 202]. The minutes of a

special directors' meeting on November 29, 1940, contains the following entry [R. 247-248]:

> "The Secretary (defendant Ballagh) reported that he had been advised by Director Dulin that he would be unable to attend the meeting and that he hoped the same would be adjourned until the following week so that he could be in attendance. It was pointed out to the Directors that there were certain matters which should be completed before the end of the current fiscal year of the company on November 30, 1940, and it was agreed that only such matters would receive attention and that all other matters for consideration would be placed before the Board at an adjourned meeting when Director Dulin could be in attendance."

The record is wholly devoid of any evidence whatever that anything was ever done violative of Mr. Dulin's complete rights as a director and stockholder.

At the top of page 5 of appellant's brief it is said that defendants were employed only as "President and General Manager" (Miller) and "Secretary and Treasurer and Sales Manager" (Ballagh) according to the minutes which appear in evidence as Plaintiff's Exhibit 1. As to the year 1939 and defendant Ballagh, the reference should be to R. 201 where defendant Ballagh was elected "Secretary-Treasurer" for that year. As to defendant Miller and 1939, the reference should be to R. 212 where defendant Miller was elected "President." Miller was never elected "President and General Manager" nor was Ballagh ever elected "Secretary and Treasurer and Sales Manager" as asserted by appellant for the years 1939, 1940 and 1941 which are in question here, but were for

each such year elected merely as "President" and "Secretary and Treasurer," respectively [R. 200, 238, 267]. In the same paragraph at the top of page 5 it is said "the defendants were employed only in the capacities above stated. *They were not employed as research men or inventors.*" (Emphasis appellant's.) And on page 6 of its brief appellant says:

> "Although the defendants in the trial court did not expressly concede that they were forced to resort to their claimed services as inventors in order to justify the amounts of their salaries, they did in several ways impliedly make such a concession."

This is a gratuitous and false assertion not justified by anything whatever in the record and it is furthermore wholly immaterial; that the defendants were conducting experiments and working as inventors was at all times known by all stockholders, directors and interested parties as the record shows and at numerous directors' meetings the progress of experimental work is referred to and discussed [R. 170, 186, 189, 194, 202], the legal effect of all of which will be hereinafter discussed.

Appellant asserts in the second paragraph on page 5 of its brief that the Board was "dominated" by Ballagh and Miller who "dictated" the policy of the corporation and reference is made to certain oral testimony. Mr. Ballagh testified that the company policies were outlined by the president and himself "subject to the action of the board" [R. 354]. Mr. Miller testified that the policies were outlined by himself "within my realm as president and with the approval of the board" and that Mr. Ballagh directed the policies in his own department [R. 381] just

exactly, we submit, as is done in any other corporation. It is next stated on page 5 that the new board, over the objections of Dulin representing plaintiff, "did three things of importance." First, it is said, it renounced the royalty agreement [Exhibits 15-a, 15-b, 15-c, and 15-d] with plaintiff corporation. This it did by advice of counsel as a pure legal and business proposition, on the theory that its monopoly under the Bettis patent having failed when that patent was declared invalid, it should no longer dissipate funds of the corporation by paying royalties for something it was not receiving. Surely this is consistent with defendants' duty to the corporation as its directors and Dulin's position in this regard was consistent only with his interest in plaintiff Byron Jackson & Co. which desired to continue receiving royalties at the expense of defendant corporation whether plaintiff was entitled to them or not. It is stated that, secondly, defendants discontinued paying dividends. This is true and there were many reasons why it should have discontinued to pay them at the time, as the record reveals [R. 361, 382, 383, 384]. Thirdly it is asserted that marked increases, being those complained of by plaintiff, were made in the salaries of Ballagh and Miller. This is true and the responsibilities and duties as well as the value of the service of both Mr. Ballagh and Mr. Miller were tremendously increased.

Just as soon as the Bettis patent was declared invalid the sales of the commodity which had constituted the corporation's principal stock in trade tremendously slumped [R. 478, 479, 480].

It was realized by the directors of the corporation that substituted articles must be developed and the duty of doing this devolved upon defendants Ballagh and Miller. They responded to this duty [R. 401, 431, 432, 433, 434, 435, 440, 449].

And as the result of the inventions which they did develop commencing with the end of the year of 1938 the volume of business and profits of the corporation were not only maintained but increased which otherwise would not have been the case [R. 126, 151, 199, 235].

At the conclusion of its purported statement of facts, (App. Br. p. 7), appellant asserts that the two questions involved in this appeal are:

> "(a) Were the salaries of Ballagh and Miller excessive? and
>
> (b) Did the plaintiff waive its right to so claim?"

If these were the only questions in the case there would be nothing for the Court to do but to dismiss the appeal. The gravamen of plaintiff's case is fraud and conspiracy and the payment of allegedly excessive salaries *as the result thereof*. Unless the fraudulent conspiracy is proven, plaintiff's whole case must fall to the ground and the statement just quoted would seem to be a waiver of the allegation of fraud and tortious wrong in the complaint.

ARGUMENT.

The Scope of the Reviewing Power of the Circuit Court of Appeals on This Appeal.

At page 42 of appellant's brief the following statement appears:

> "We point out that not only is this an equity case, but also that under rule 52(a) of the Rules of Civil Procedure, where findings are made by the court without a jury, the appellate court is not limited to the mere question whether there is any substantial evidence to support the findings, but may set them aside if against the clear weight of evidence (State Farm Mut. Automobile Ins. Co. v. Bonacci, 111 Fed. (2d) 412)."

We challenge the statement that this is an equity case in the first place, and, in the second place, the correctness of the statement relative to the power of the Appellate Court in reviewing questions of fact and findings of fact made by the trial Court where a law action is tried to the Court as the trier of fact, rather than to a jury.

Considering the latter of these two propositions first, we believe the true rule as to the power of the Appellate Court to review facts and findings of fact made by the trial Court, is correctly stated in the following cases:

Sundt v. Turman Oil Co. (C. C. A. Tex., 1940), 107 F. (2d) 762;

Great Atlantic & Pacific Tea Co. v. Grosjean (1937), 301 U. S. 412, 420, 57 S. Ct. 772, 81 L. Ed. 1193, 112 A. L. R. 293, rehearing denied 302 U. S. 772, 58 S. Ct. 3, 82 L. Ed. 599;

Borden's Farm Products Co. v. Ten Eyck (1936), 297 U. S. 251, 261, 56 S. Ct. 453, 80 L. Ed. 669;

Murphy v. Sun Oil Co. (C. C. A. Tex., 1937), 86 F. (2d) 895. Cert. den. 300 U. S. 683, 57 S. Ct. 754, 81 L. Ed. 886, wherein the Court said:

"The evidence other than documentary was all given orally. The District Judge heard the witnesses, and we are bound by his findings unless they are unreasonable, *that is, wholly without support in the evidence.* We cannot find them so." (Italics ours.)

Western Union Telegraph Co. v. Nester (C. C. A. Cal., 9th Cir., 1939), 106 F. (2d) 587. Certiorari granted ...... U. S. ......, 60 S. Ct. 468, 84 L. Ed. ....

This case was subsequently reversed by the Supreme Court of the United States, 309 U. S. 582, 84 L. Ed. 960 on other grounds.

Cherry-Burrell Co. v. Thatcher (C. C. A. Mont., 9th Cir., 1940), 107 F. (2d) 65. [See Appendix p. 1.]

Storley v. Armour & Co. (C. C. A. 8th, 1940), 107 F. (2d) 499. [See Appendix p. 1.]

Crowell v. Baker Oil Tools, Inc. (C. C. A. 9th), 99 F. (2d) 574. [See Appendix p. 2.]

Incidentally in the case of

State Farm Mut. Automobile Ins. Co. v. Bonacci, 111 Fed. (2d) 412,

the only case cited by appellant in support of its assertion, the facts are that the record in the trial court consisted largely of documentary evidence as distinguished from oral testimony, which fact the Circuit Court of Appeals for the Eighth Circuit specifically mentions in justification of its reversal of the findings of fact of the District Court. [See Appendix p. 3.]

Consequently the case cited is not authority for the power of the appellate Court to review facts found by the trial Court in a case where the testimony is principally oral as in the case at bar.

This Is an Action at Law and Not a Suit in Equity.

The question as to whether this is a suit in equity or an action at law is important not only with reference to the power of the appellate Court to review findings of facts but also in determining upon which party the burden of proof rests and the extent and character of that burden of proof. Respondents contend that the case is an action at law in the nature of a tort action, the alleged wrong being grounded in fraud and conspiracy to commit fraud. The remedy sought is a money judgment in favor of the corporation in a categorically definite amount. No accounting, injunctional relief or other equitable remedy of any kind is asked nor is any necessary in order to afford plaintiff the relief which it seeks, assuming only that it proves its allegations of fact by a fair preponderance of the evidence as in other tort actions.

To determine whether the action is legal or equitable, resort must first be had to an examination of the complaint itself.

The only allegations in the complaint entitling plaintiff to any relief (other than formal allegations relative to the parties, jurisdiction, stock ownership in defendant corporation, prior demands, etc.) are contained in paragraphs IV, V, VI, VII, VIII, and IX.

In paragraph IV it is alleged that the Board of Directors consisted of five persons of whom three were Dulin, president of plaintiff, defendants Ballagh and Miller "and other persons who were selected by such directors by, and in fact were and are representives of, the said Ballagh and the said Miller upon the said board"; and

that defendants Ballagh and Miller "by means of their said stock ownership and by means of their said representation upon the Board of Directors of said corporation by themselves and by their said representatives * * * at all times * * * have dominated, controlled and directed, and do now dominate, control and direct each and every of the acts and doings of the said defendant corporation." Paragraph V alleges that the defendants Ballagh and Miller "have fraudulently and unlawfully connived, cooperated, schemed and conspired and do now fraudulently and unlawfully connive, cooperate, scheme and conspire in directing the affairs of the said corporation for their own ends as distinguished from the well-being of said corporation and the interests of plaintiff as a minority stockholder thereof and for their own profit * * *."

Paragraph VI merely alleges that, as a part of the scheme and conspiracy alleged in paragraph V, defendants Ballagh and Miller as directors of defendant corporation together with the other directors (excepting Dulin), who are their "representatives," declared and paid to defendant Ballagh excessive salary and compensation in *certain specific amounts* for the year 1939, 1940 and 1941. The paragraph does not seek an accounting but alleges *in exact figures* what plaintiff deems to be reasonable compensation for defendant Ballagh for each year, the amount actually paid as such and *the exact amount of the claimed excess.*

Paragraph VII is identical in language with paragraph VI excepting that it relates to the compensation paid to defendant Miller.

Paragraph VIII alleges that plaintiff has received no dividends from defendant corporation at any time since February 15, 1939, and that, on information and belief, defendants Ballagh and Miller arranged to be paid alleg-

edly excessive salaries for the three years in question for the purpose of depriving plaintiff of dividends.

Paragraph IX alleges that "said defendants Ballagh and Miller are indebted to said defendant corporation in at least the sum of $41,416.66, no part of which has been repaid by the said Ballagh or by said Miller or by either thereof to the said corporation." This is obviously nothing but a common count at law in *indebitatus assumpsit* for a specific amount which is the exact difference between the amounts alleged to have been actually paid to defendants Ballagh and Miller in the years 1939, 1940 and 1941 and the amounts alleged to have been reasonable compensation for each of them for these years as set forth in paragraphs VI and VII.

The prayer for relief asked for judgment "against said defendants Ballagh and Miller in the sum of $41,416.66 with interest, etc." It will be noted that separate judgments are not asked against the defendants Ballagh and Miller notwithstanding the fact that the excess payments claimed as to each of them in paragraphs VI and VII differ widely, the excess as to Ballagh claimed in paragraph VI being $30,166.66 whereas the excess claimed as to Miller in paragraph VII is $10,250. A joint judgment against both is sought in the full amount exactly as a judgment for the full amount of plaintiff's damage would be sought against joint tort feasors in an action at law. This fact is important in determining whether the action is legal or equitable, and also in considering the equitable status of a plaintiff which presumes to seek in a court of equity a judgment in the sum of $41,416.66 against a defendant who, even according to its own allegations, can owe no more than $10,250 and against another who, according to its allegations, can owe no more than $30,166.66.

Much loose language appears in the opinions of Courts in cases where derivative actions are brought by minority

stockholders to recover allegedly excessive compensation paid to officers and directors, either on behalf of themselves "and all other stockholders similarily situated" or on behalf of the corporation itself as in this case, to the effect that such actions are equitable in their character. Having read literally hundreds of such cases, we confidently state to the Court that in no case have we found an action of this character treated as a suit in equity where some equitable relief has not been sought in the complaint or applied by the Court. The usual equitable relief sought or applied in such cases is an accounting. This is sometimes accompanied by injunctional relief of some character and in many cases a receiver is sought. In the case at bar, however, as appears clearly from the face of the complaint, no equitable relief of any kind is asked nor is any necessary to afford plaintiff the complete remedy it seeks. The complaint cannot possibly be regarded as stating a cause of action other than at common law to recover damages against joint tort feasors, the tort consisting of a fraudulent conspiracy.

The Court's official record shows that on Friday, July 3, 1942, "this cause came on for further trial without a jury" [R. 35] and on July 6, 1942, "this cause coming on for further non-jury trial, etc.", both of which entries are strongly corroborative of the idea entertained by all parties at the time that the case was one at law being tried to the court as the trier of facts rather than to a jury.

Under these circumstances the Courts, wherever the question has been raised, have uniformly held such derivative actions brought against corporate directors to be actions at law and not suits in equity. This question occasionally becomes highly important and fundamental. For example, if the action is one at law the defendant should not be deprived of his constitutional right to a jury trial. In some states a different statute of limitations applies

to actions at law and to suits in equity and, in some, as in California, in a suit in equity an appeal lies to the Supreme Court of the State, whereas in an action at law, the appellate Court of last resort is the intermediate appellate court. Thus the Courts have been called upon to pass upon the question as to whether actions of this character are at law or in equity and, tested by the standards laid down in those decisions an examination of the complaint in this case establishes conclusively that this is an action at law tried to the Court rather than to a jury with the apparent acquiescence of both sides.

In the early case of

O'Brien v. Fitzgerald (N. Y.), 38 N. E. 371,

the receivers of a banking corporation, themselves the creatures of equity, sued directors to recover back amounts which it was alleged the corporation had lost by reason of their wrongful conduct. Obviously the plaintiff receivers were suing in a derivative or representative capacity for the benefit of the corporation. The Court says:

> "There is no suggestion that any equitable relief is essential to a full and complete redress, and no facts are stated which indicate a need of such intervention. It is not averred that a discovery is requisite to the completeness of the remedy. On the contrary, the acts of negligence are asserted as fully known, and capable of proof. It is not alleged that an accounting is necessary to ascertain the damages, but these are claimed as a definite and fixed sum, resulting directly from the negligent acts of the defendants. It is not asserted that such defendants are severally liable for separate and personal misconduct, and in separate and different amounts, although that is a reasonable inference from the facts stated in the complaint, but it demands judgment against all and against each for the full amount claimed."

We submit that the foregoing language is exactly applicable to the case at bar. Much more might be quoted from the opinion to make the analogy even more complete. The Court of Appeals of New York held that the action was purely legal and in no sense equitable.

In

Cwerdinski v. Bent, 11 N. Y. Supp. (2d) 208,

which was a suit by a minority stockholder against the directors of the Bethlehem Steel Corporation to recover for the corporation certain very large bonuses paid to officers and where a six-year statute of limitations applied to actions at law whereas a ten-year statute of limitations was applicable to suits in equity, the result was the same. [See Appendix p. 3.]

The authorities which govern the question in the case at bar are collated and discussed ably by Judge O'Brien in

Potter v. Walker, 276 N. Y. 15, 11 N. E. (2d) 335.

The Court held that the action was legal and not equitable and that the six-year and not the ten-year statute of limitations applied. Plaintiff, as a minority stockholder in the Pan American Petroleum and Transport Co., brought a derivative action against directors of the corporation for acts allegedly committed by them, including the allegedly wrongful payment to one of them of the sum of $150,000. In the complaint an accountting is asked but the Court holds that, as to this particular cause of action, none is needed since the amount of the alleged loss to the corporation was directly asserted in the complaint, that consequently an action at law affords a complete remedy, no resort to equity is required, the action is therefore legal and not equitable and the six-year and not the ten-year statute of limitations applies. In the

course of the opinion the New York Court of Appeals quotes from

> *Wallace v. Lincoln Savings Bank* (Tenn.), 15 S. W. 448, 24 Am. St. Rep. 625,

an opinion written by Mr. Justice Lurton, later a distinguished member of the Supreme Court of the United States. [See Appendix p. 4.]

The same question arose in the case of

> *Becker v. Empire Power Co.,* 31 N. Y. Supp. (2d) 914.

This was a suit by minority stockholders against officers and directors of a corporation "*for an accounting in equity*" to recover alleged unlawful profits obtained by them at the expense of the corporation. The Court held the action to be one at law and not in equity. [See Appendix p. 5.]

The decision of the Court of Appeals of the State of New York in

> *Dunlop v. Dunlop,* 34 N. E. (2d) 344,

was followed in the case just cited. The opinion is *per curiam.* [See Appendix p. 5.] The obvious effect of this opinion is that where no equitable remedy is required as in the case at bar, the action is one at law and not one in equity even though it be one brought by a minority stockholder in a derivative capacity to recover profits gained by corporate directors who "have profited in any degree through a breach of their fiduciary duties" which is the claim here.

An early New York case of the same character,

> *Dykman v. Keeney,* 48 N. E. 894,

involved the question of the right of defendants to a trial by a jury. The Court in a well reasoned opinion dis-

cusses the situation at length, cites and quotes many authorities and holds that an action at law affords a complete remedy, that the defendants should not be deprived of their constitutional right of a trial by a jury and that the action is strictly legal and in no sense equitable.

The same question arose in a different connection in the case of

Gormley v. Slicer (Ga. Sup. Ct.), 172 S. E. 23.

It was an action by the State Superintendent of Banks on behalf of depositors, stockholders and creditors of a defunct trust company against the latter's trustees who, the opinion says, occupy the same status as the directors of a corporation, to recover losses occasioned by their negligence in administering the affairs of the bank. If the action was equitable in its nature an appeal would lie direct to the Supreme Court of the State, whereas if it were legal in character, such an appeal would not lie. The question was certified to the Supreme Court which held the action to be purely legal in character although the reference to that Court shows that the case involves complicated and numerous items covering a period of years which it would be difficult to present to a jury. [See Appendix p. 6.]

In

Potter v. Walker, 287 N. Y. Supp. 812,

which was later affirmed by the Court of Appeals in the case of the same title reported in 11 N. E. (2d) 335, *supra,* the whole question is most thoughtfully and carefully analyzed and discussed and with the same result. [See Appendix p. 6.]

In

Emerson v. Gaither et al. (Md.), 64 Atl. 26,

the Court quotes from Clark and Marshall on Corporations and Judge Thompson's article on corporations in 10 Cyc. [See Appendix p. 8.]

The same principle is recognized by the Federal courts.

Corsicana Nat. Bank v. Johnson (C. C. A. 5th), 218 Fed. 822,

was an action against an officer of a national bank to recover alleged losses resulting from the defendant's violation of a Federal banking statute. The Court reached the same result on this question. [See Appendix p. 9.]

See also the majority opinion by Mr. Justice Holmes in

Curtis v. Connly, 257 U. S. 260, 66 L. Ed. 222.

In those states where courts have held that a stockholder's derivative suit to impose liability on directors is one in equity (although in every such case we have been able to find, an equitable remedy is either sought or applied as we have already stated), the rule seems to prevail that a corporation director is a trustee of the corporation, its stockholders and creditors to the same extent and with the same duties and liabilities as is a trustee of an express trust.

The better rule is that, while a trustee occupies a fiduciary relationship to the corporation, its stockholders and creditors, that relationship is one of agency and in the director's dealings with the corporation and its property his fiduciary liability is the same as that of an agent to his principal and not that of a trustee of an express trust to his *cestui que* trust. That is the rule in California.

In

Ballantine's Manual of Corporation Law and Practice, 1930 Edition, Sec. 122,

it is said:

"As was stated in a former section, it is sometimes said that the directors and other officers of a corporation are trustees for the corporation, but, strictly speaking, this is not true. The relation is that of principal and agent, and is governed by substantially the same rules as govern a similar relation between material persons."

In the recent case of

Bainbridge v. Stoner, 16 Cal. (2d) 423,

an opinion by the Supreme Court of California decided in 1940, which was a suit brought by directors and minority stockholders of a corporation to have another director declared trustee of certain mining claims for the benefit of the corporation and its stockholders, the Court says with reference to the status of a corporate director:

"However, strictly speaking, the relationship is not one of trust, but of agency, although it has been held that a director must comply with the requirements of Section 2230 of the Civil Code relating to trustees."

This appears to be the last pronouncement of the Supreme Court of California on the subject.

It must be admitted that, in the case at bar, California law is controlling. Defendant is a California corporation. The two individual defendants are citizens and residents of that state and all of the transactions complained of occurred therein. It consequently seems conclusive that the status of the defendant directors is that of agents for the corporation, that the action against them is purely one at law to recover a definitely alleged sum of money in a joint judgment against them by way of damages allegedly

sustained by the defendant corporation as the result of their tortious conduct amounting to a fraud committed upon it and, as the result of which, it is claimed the defendant corporation's stockholders, including plaintiff, have indirectly suffered. All of this being true, it necessarily follows:

First, that the reviewing power of the Appellate Court as to issues of fact and the findings made thereon by the trial court, are narrowed and restricted as compared with what would be the case if the suit were one in equity; and

Second, that the burden rests upon plaintiff to prove the alleged tortious wrong claimed to have been committed by the individual defendants and the resulting damage by a fair preponderance of the evidence just as in any other tort action at common law.

Irrespective of Whether the Case at Bar Be One at Law or in Equity, the Burden of Proof Is Upon the Plaintiff.

The first section of the argument in appellant's brief, pages 22-25, inclusive, consists of an attempt to establish that:

> "due to the relationship of the (individual) defendants to the corporation it was not only unnecessary for plaintiff to establish fraud, but a presumption arose in plaintiff's favor that the salaries were excessive."

The foregoing seems to us a most extraordinary statement and means that in any case a minority stockholder in a corporation might commence an action by drawing a complaint alleging fraud and the payment of excessive salaries to officers and, as the result thereof and by filing and serving this complaint, he would, *ipso facto*, have made out a *prima facie* case.

Later the following statement appears:

> "When directors of a corporation are in this position (by which we suppose is meant that they are also majority stockholders) a minority stockholder, in order to force restitution by the directors to the corporation, need not establish fraud; there, also, arises a presumption that the salaries were unreasonable and the burden of proof is upon the directors to show the contrary."

According to appellant, no proof whatever by plaintiff is required either to establish fraud or any other wrongdoing nor that the salaries complained of are excessive. The mere allegations in the complaint are all that is required and, as will be seen, are all that plaintiff has produced in the case at bar to support its contention.

Obviously this is not the law and to contend that it is, certainly should throw discredit upon appellant's entire case.

As stated, this case and the conduct of the parties herein are governed by the law of the State of California.*

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*Section 311, C. C. P., provides in part:

"No contract or other transaction between a corporation and one or more of its directors * * * shall be either void or voidable by reason of the fact that such director or directors are present at the meeting of the Board of Directors or a committee thereof which authorizes or approves such contract or transaction or that his or their votes are counted for such purpose, if:

"(a) the fact of such * * * financial interest be disclosed or known to the Board of Directors or committee and noted in the minutes and the board or committee authorize, approve or ratify such contract or transaction in good faith by a vote sufficient for such purpose without counting the vote or votes of such director or directors; or

"(b) the fact of such * * * financial interest be disclosed or known to the shareholders and they approve or ratify such contract or transaction in good faith by a majority vote or written consent of shareholders entitled to vote; or

"(c) the contract or transaction be just and reasonable as to the corporation at the time it was authorized or approved.

"Such common or interested directors *may be counted in determining the presence of a quorum at such meeting.*" (Italics ours.)

All of the essentials of this statute were complied with in connection with each corporate action complained of by plaintiff. The sole claim which plaintiff can make under this statute is under subsection (c) on the issue as to whether the transactions complained of were "just and reasonable as to the corporation" at the time they were authorized and approved. Plaintiff says they were not and the defendants say they were. Obviously, it is the duty of plaintiff to sustain its contention by a preponderance of the evidence as in other cases.

As the Court knows, there are in the State of California certain statutory presumptions, many of which are directly applicable to the situation here.*

Each and every one of these presumptions cloaks the two individual defendants in this case and, taken as a whole, are sufficient to surround the transactions complained of and every element thereof. Number 1, until it has been overthrown by evidence, absolves them from the tortious fraud, conspiracy and wrong alleged by plaintiff. Number 7 establishes, *prima facie,* and until overthrown by evidence produced by plaintiff, that the compensation paid to them was due them. Number 11, *prima facie*, establishes that the compensation received by them belongs to them until the plaintiff has proven otherwise. Number 15 cloaks the official acts of directors of defendant corporation with regularity until plaintiff has proven irregularity and fraud by evidence. Number 19 estab-

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*Section 1963, C. C. P., defines forty rebuttable presumptions, among which are:

"1. That a person is innocent of crime or wrong;
"7. That money paid by one to another was due to the latter;
"11. That things which a person possesses are owned by him;
"15. That official duty has been regularly performed;
"19. That private transactions have been fair and regular;
"20. That the ordinary course of business has been followed;
"33. That the law has been obeyed;
"39. That there was a good and sufficient consideration for a written contract."

lishes, *prima facie*, the fairness and regularity of all the corporate acts complained of by plaintiff until it has satisfied the burden of proof devolving upon it by evidence, and the same thing is true of Number 20. Number 33 establishes *prima facie* that the defendants in doing whatever they have done acted lawfully.

A resolution of a corporate board of directors for employment and fixing compensation is a contract in writing and has mutuality.

> 27 *C. J.*, Sec. 307, pp. 257-258;
>
> *Western Timber Co. v. Kalama River Lumber Co.* (Wash.), 85 Pac. 338, 114 Am. S. R. 137, 6 L. R. A. (N. S.) 397, 7 Ann. Cas. 667.

Therefore, there is here a statutory presumption that both defendants Ballagh and Miller rendered "a good and sufficient consideration" for the compensation paid them by defendant corporation.

Solely as the result of the statutes of the State of California, it is clear that the burden is upon the plaintiff to prove both elements of its alleged case, that is; first, the fraudulent conduct of the individual defendants, and; second, the alleged overpayments for their services: both by a preponderance of the evidence.

Indeed this is the universal rule.

In

> *Presidio Mining Co. v. Overton* (C. C. A. 9th Cir.), 261 Fed. 933,

a case decided by this Court in 1919, in which the opinion was written by Mr. Justice Morrow and which was a suit brought by minority stockholders for a variety of types of equitable relief, including an accounting, injunctive relief and a receivership and therefore necessarily cog-

nizable in equity, the Court says on the question of burden of proof (page 940):

> "The minority stockholder is entitled to the protection of a court of equity against the illegal and fraudulent acts of the majority; but the misconduct of the majority must be clearly established to justify the court in such interference. *Here, as elsewhere, fraud is not presumed, but must be proved.* Lewisohn v. Anaconda Copper Min. Co., 26 Misc. Rep. 613. 56 N. Y. Supp. 807-818." (Italics ours.)

And again at page 960 of the opinion it is said:

> "The burden of proof was upon the plaintiffs to prove the illegal and fraudulent character of the salaries paid to the directors and officers in San Francisco."

It will be borne in mind that the foregoing was admittedly an equity case and not purely an action at law, as is the case at bar.

In

> *Gamble v. Queens County Water Co.* (N. Y.), 25 N. E. 201,

a minority stockholder's suit seeking to enjoin the issuance of corporate stock and bonds and in an opinion by Mr. Justice Peckham, later of the United States Supreme Court, which case is cited with approval by the California District Court of Appeal, Third Appellate District. In *Fornaseri v. Cosmosart Realty Corp.*, 96 Cal. App. 549, later to be commented on, the New York Court of Appeals places the burden of proof upon the plaintiff and says that "a case must be made out which plainly shows" that the actions complained of are wrongful and not for the best interests of the corporation.

Spiegel v. Beacon Participations, Inc. (Mass.), 8 N. E. (2d) 895,

was a minority stockholder's suit in equity to recover from the directors alleged loss to the corporation resulting from the purchase for the corporation of a large note which it was claimed was worthless. On the issue of burden of proof the court says:

> "Commonly, the burden of proof in a suit by or in behalf of a corporation against its officers or directors is on the plaintiff to show misconduct." (Citing many cases, p. 905.)

And again:

> "As already pointed out in our opinion the burden of proof is on the plaintiff to show the loss sustained by the defendant by the misconduct of the several defendants."

Schmitt v. Eagle Roller Mill Co. (Minn),

which is a minority stockholder's case of the same character, is to the same effect and it is there said:

> "There is no presumption that the directors acted in bad faith or unjustly." (P. 282.)

Nahikian v. Mattingly (Mich.), 251 N. W. 421,

was an action brought by three minority stockholders to force a director and officer to repay alleged excessive salaries, unauthorized expense moneys, royalties received on a patent, to assign a patent to the company, to turn over certain shares of stock held by him in trust for the company, to pay indebtedness owed by him to the company and to remove him as president, director and general manager. The court holds that the burden of proof is upon the plaintiff. The court's remarks, not only on

the issue of burden of proof but on the entire question of excessive salary payments, are so pertinent as to justify quoting. [See Appendix p. 10.]

In

Bates Street Shirt Co. v. Waite (Me.), 156 Atl. 293,

which was a suit in equity to recover from former directors money alleged to have been fraudulently converted to their use by way of alleged excessive salaries and otherwise, or illegally expended by them, the court says:

> "The burden of proving that the salaries are excessive is on the complainant. Presidio Mining Co. v. Overton (C. C. A.), 261 Fed. 1023 and if fraud is alleged the proof must be clear and convincing." (Citing cases, p. 298.)

And, at the conclusion of the opinion:

> "Plaintiff has not sustained the burden of proving these charges. On the contrary, there is much to prove that defendants conducted the business of the corporation with fidelity and integrity."

The same rule is announced in

Chapman v. Troy Laundry Co. (Utah), 47 Pac. (2d) 1054,

which was a derivative suit brought by minority stockholders against corporate directors seeking to cancel certain shares of stock allegedly improperly and fraudulently issued. [See Appendix p. 12.]

In

Savory v. Berkey (Minn.), 2 N. W. (2d) 146,

another minority stockholder suit seeking to recover from corporate directors for the benefit of the corporation,

losses allegedly sustained by the latter as the result of misappropriation of corporate funds, the court says:

> "With the charges of misappropriation and wrong-doing made by plaintiff he, of course, had the burden of proof."

> *Bodell v. General Gas & Elec. Corp.* (Del.), 132 Atl. 442,

a suit of a similar character, the court held similarly. [See Appendix p. 12.]

In

> *Cole v. National Cash Credit Ass'n.* (Del.), 156 Atl. 183,

which is a suit of the same general type, clearly in equity and seeking injunctional relief, the result is the same. [See Appendix p. 12.]

> *Karasik v. Pacific Eastern Corp.* (Del.), 180 Atl. 604,

was a suit in equity for injunctional relief by corporate stockholders against officers and directors of the corporation, claiming the squandering and wasting of large amounts of corporate money. The court holds the burden of proof to be on plaintiffs. [See Appendix p. 13.]

And in

> *Anderson v. Bean* (Mass.), 172 N. E. 647, 72 A. L. R. 959,

which was a suit by certain beneficiaries of a trust against the trustee, in which, it should be pointed out, the defendant was actually the trustee of an express trust and not merely an agent as are corporate directors, the result is the same. [See Appendix p. 13.]

See also:

Beha v. Martin (Ky.), 171 S. W. 393.

In

Venus Oil Corp. v. Gardner (Ky.), 50 S. W. (2d) 537,

which was a case identical in principle with that at bar, there was a judgment in favor of plaintiff in the trial court for the return of salaries in the sum of $27,625 which the Appellate Court reversed on appeal, saying in the second paragraph of the opinion "the burden is upon the objecting stockholders to establish affirmatively that the compensation allowed was unreasonable and excessive. Beha v. Martin, *supra*."

Winberg v. Camp Taylor Dev. Co. (Ky.), 95 S. W. (2d) 261,

is substantially on all fours with the case at bar and the holding is the same. [See Appendix p. 14.]

In the complaint in this case there were allegations of fraud, irregularity, conspiracy, etc., and the court intimates that they are all mere conclusions without the allegation of any ultimate facts to support them and, as such, subject to demurrer. We submit that the same thing is true of the allegations of the same character in the complaint here.

In

Borg v. International Silver Co. (D. C. N. Y.), 11 Fed. (2d) 143,

in which an injunction was sought by minority stockholders to prevent the sale of corporate stock, the court says:

> "* * * and while the plaintiffs impute to the directors an ulterior purpose, and allege that they are

> not acting in the interest of the company, from all that appears there may be an honest difference of opinion as to what is best for the company. The position of director is one of trust for the benefit of the stockholders, and, until the contrary is clearly shown, it must be assumed that they are actuated solely by what, in their judgment, is best for the stockholders."

in denying plaintiff's motion for a temporary injunction. This decision was affirmed by the Circuit Court of Appeals for the Second Circuit in

Borg v. International Silver Co., 11 Fed. (2d) 147. [See Appendix p. 14.]

In

Noel v. Parrott (C. C. A. 4th), 15 Fed. (2d) 669, Cert. den. 47 S. Ct. 457, 273 U. S. 754, 71 L. Ed. 875,

which was a suit by a taxpayer against the Collector of Internal Revenue, the plaintiff claiming that certain money received by him from a corporation was a gift and, as such, not taxable as income, the court says there is a presumption of regularity and honesty attending the official action of corporate directors. [See Appendix p. 15.] And this presumption was indulged by the court even though the directors were not parties to the action and certainly not in the position of defendants as to whom the well-nigh universal rule is that a plaintiff must prove his case by a preponderance of the evidence in order to prevail.

Gray Corp. v. Meehan (C. C. A. 1st), 54 Fed. (2d) 223,

is to the same effect. [See Appendix p. 15.]

It therefore seems conclusive that the Federal courts follow the usual rule that where irregularities or fraud

are charged against corporate directors, the latter are protected by a presumption of regularity and honesty in their official acts which must be overthrown by evidence and that, in addition, the burden of proof is on the plaintiff; and this must necessarily be so where the transactions are governed by the laws of a state in which the same rule prevails, as is true in the case at bar.

The California decisions in both the Supreme Court and District Courts of Appeal follow the general rule already stated.

In

Snediker v. Ayres, 146 Cal. 407,

the California Supreme Court, after quoting portions of Section 2230 of the Civil Code, *supra,* says:

> "The plaintiff alleged fraud and collusion on the part of the directors, and the burden was on him to establish these allegations. The findings show the contrary."

Certainly no language could be more apt than the foregoing to dispose of plaintiff's contention relative to the burden of proof in the case at bar.

In

Fornaseri v. Cosmosart Realty etc. Corp., 96 Cal. App. 549,

plaintiffs were stockholders and creditors of the defendant corporation in which the corporate directors were joined as defendants and it was sought to recover from them certain funds allegedly held in trust for the corporation which had been realized from the sale of a certain lease and option belonging to the corporation. The court holds that the presumptions favor the defendants and the burden of proof is on the plaintiffs. [See Appendix p. 16.]

In

Michaels v. Pacific Soft Water Laundry, et al., 104 Cal. App. 366,

which was a suit by stockholders questioning the validity of a corporate election and in which a rehearing by the District Court of Appeal and a hearing by the Supreme Court of the State were both denied, the court reaches the same result. [See Appendix p. 16.]

And again in

Clark v. Oceano Beach Resort Co., 106 Cal. App. 574,

plaintiff stockholder sought to enjoin the sale of his stock in the corporation contemplated because of his failure to pay an assessment theron. It was claimed that the assessment was levied as the result of a conspiracy between certain of the directors with the intent to oust other stockholders and obtain the control of the corporation and the trial court so found. The Appellate Court reverses the trial court, and announces the same rule. [See Appendix p. 17.] In this case also a petition for rehearing before the same court and a hearing by the Supreme Court of the State were denied. It would seem conclusive that the rule in California is as contended by respondent and that this Court in passing upon a purely California transaction involving the internal affairs of a California corporation is bound by this rule.

Appellant's Cases Distinguished.

To support its extraordinary contention that no proof is necessary either to establish fraud or that the salaries complained of were excessive and, in effect, that all that is necessary to cast on defendants the burden of disproving these claims is to commence an action in which the complaint alleges them, appellant first cites the case of

Stratis v. Anderson (Mass.), 150 N. E. 832,

from which case it quotes an excerpt which we submit from a reading of the entire case is wholly misleading and deceptive. This was a minority stockholder suit seeking to recover alleged excessive salaries for the benefit of the corporation. The opinion starts out by saying:

> "The case was referred to a master. Since there is no report of the evidence, his findings of fact must be accepted as final and true."

Immediately preceding the excerpt quoted by appellant from this case the court says:

> "It is not necessary to inquire nicely into the relative rights of the parties where the majority of the directors who are disinterested fix a salary by vote for an associate in participating in the vote."

That is exactly what occurred in the case of each vote of the directors in fixing the salaries of the individual defendants in the case at bar. Upon none of the ballots did the defendant officer participate in the vote fixing his own salary as the minutes show and as will be subsequently pointed out. In the *Stratis case* there were three directors, each of whom was an officer and the salary of each of whom is complained of. Each officer participated in the vote as to his own salary. The books are full of cases condemning directors for participating in the votes determining their own salaries. That, however, is not the case here. Neither Mr. Ballagh nor Mr.

Miller participated in any vote relative to his respective salary, which fact totally distinguishes the case at bar from the *Stratis case* as the Massachusetts court says in the language above quoted. In the excerpt quoted by appellant from the *Stratis case* are cited many cases which it is claimed support the position asserted by appellant. We can say confidently that none of them does as applied to the facts in the case at bar.

In the case of

> *Von Arnim v. American Tube Works* (Mass.), 74 N. E. 680,

a minority stockholder suit against corporate officers and directors for alleged misappropriation of funds, the court says at the commencement of its opinion:

> "Under a bill of complaint brought by a minority stockholder against the officers of the corporation for official misconduct by which its assets have been wrongly appropriated, *it is obligatory for him to allege and prove that they have failed to perform their duty, thus causing a breach of their trust;*" (Italics ours)

which obviously is directly contrary to the assertion and claim of appellant in this regard and is excellent authority for the contention of respondents.

In

> *Meyer v. Ft. Hill Engraving Co.* (Mass.), 143 N. E. 915,

next cited which was also a minority stockholder's suit seeking to recover alleged excessive salary and in which the directors were joined as defendants, there was a judgment for defendants. affirmed on appeal because of plaintiff's failure of proof and on the issue of the burden of proof the court says:

> "The burden of proving mismanagement, and alleged wrongful appropriation of the moneys of the com-

pany *was on the plaintiff.* The judge saw and heard the witnesses upon whose evidence, in some respects conflicting, the question depended, and his finding, 'I am not satisfied the payments to Ioos, Freyer and Yeaton have been excessive,' cannot be said to be plainly wrong. Revere Water Co. v. Winthrop, 192 Mass. 455, 459, 78 N. E. 497." (Italics ours.)

This case is also excellent authority for respondents here and we suggest could hardly have been read by appellant before citing it to this Court.

Godley v. Crandall & Godley Co. (N. Y.), 105 N. E. 818,

also cited by the Massachusetts court, was a minority stockholder suit for an accounting and to compel the return of moneys distributed to officers and directors in proportion to their stock holdings and without relation to any services rendered by them. There is no word at any place in the opinion concerning the burden of proof but a fair reading and interpretation of the opinion certainly leads to the conclusion that the Court assumed the burden to be on plaintiff even though the suit was one necessarily in equity.

Green v. National Advertising, etc. Co. (Minn.), 162 N. W. 1056,

sought an accounting, the appointment of a receiver and other equitable relief and was brought by plaintiff who owned one-half of the corporate stock, against defendants who owned the other one-half. At no point in the opinion is the question of the burden of proof even referred to. We have already cited and quoted from Minnesota cases which clearly establish the rule in that state as being in accordance with the contention of respondents here.

Lillard v. Oil Paint & Drug Co. (N. J.), 56 Atl. 254

is likewise entirely silent on the question of burden of proof and the subject is nowhere even referred to in the opinion of the court and the same thing is true in the report of the same case contained in 58 Atl. 188 which is confined solely to the question of costs.

Booth v. Beattie (N. J.), 118 Atl. 257

is likewise devoid of any reference whatever to the burden of proof upon the respective parties but certain language contained therein seems particularly appropriate on the merits of the case subsequently to be considered. [See Appendix p. 17.]

The memorandum opinion in the same case reported in 123 Atl. at page 925 is likewise silent on the subject.

The last case cited in the quotation from the *Stratis case, supra,* is

Sotter v. Coatesville Boiler Works, et al. (Pa.), 101 Atl. 744.

At no point in the opinion is there even the merest reference to the question of burden of proof but the Court evidently proceeded on the theory that the burden is on the plaintiff as in other cases even though the suit is one in equity seeking an injunction. [See Appendix p. 18.]

The foregoing should effectively dispose of the case of

Stratis v. Anderson, supra,

and the cases cited by appellant in the excerpt which it quotes from that decision, all of which are, in reality, authority for respondents' position on the point being considered.

Appellant next cites

> *Geddes v. Anaconda Copper Mining Co.,* 254 U. S. 590, 65 L. Ed. 425

and quotes an excerpt from that opinion. This suit was brought by minority stockholders of the Alice Gold & Silver Mining Company, all of the stock of which had been sold to defendant Anaconda, claiming that the stock of the Alice Co. had not been properly evaluated in the transaction. Among the grounds of attack was the fact that the sale was negotiated by two boards of directors (of the two companies involved) with a common membership and for an inadequate consideration. The facts were that the purchase of the Alice Co. stock was paid for by an exchange of Anaconda stock. The Court finds that the Anaconda stock had a definite money value on the New York and other stock exchanges and "* * * when stock which has an established market value is taken in exchange for corporation property, it should be treated as the equivalent of money, * * *." Where it clearly appeared as a matter of mathematical certainty that the consideration for the purchase assessed at its money value was inadequate, the plaintiff necessarily had sustained the burden of proof and the burden was thereupon cast upon the defendant to justify it. That is all that the quoted language from the opinion means. In addition, it might be pointed out that the directors of both corporations were the same and that they all participated in the official action of both boards with resulting personal profit to themselves, whereas in the case at bar neither of the individual defendants participated in the board action affecting himself.

In the excerpt quoted the Court cites

> *Twin Lick Oil Co. v. Marbury,* 91 U. S. 587, 23 L. Ed. 328.

There is nothing in the opinion relative to the burden of proof.

Thomas v. Brownville etc. R. Co., 109 U. S. 522, 27 L. Ed. 1018

is also cited. Here also there is no reference to the subject of burden of proof but the Court does say relative to the allegations of fraud made by plaintiffs "these allegations are proved beyond question, and the Circuit Court held the contract void and the bonds issued in fulfillment of it also void, and dismissed the bill." This must surely mean that plaintiffs not only sustained the burden of proof but proved their case conclusively by evidence.

The next case cited in this excerpt is

Corsicana National Bank v. Johnson, 251 U. S. 68, 64 L. Ed. 141.

This was an action brought by a national bank against a former director to hold the latter liable in damages for allegedly making illegal loans. Not only is this case no authority for appellant's contention relative to the burden of proof but it is direct authority contrary thereto as the language of the opinion in several places clearly indicates. In this regard it is perhaps sufficient to quote the second section of the syllabus which reads:

> "What weight should be given to substantial evidence tending to support the plaintiff's view of disputed facts is for the jury, not the court, to determine."

Appellant next cites and quotes from the case of

Davids v. Davids, 120 N. Y. Supp. 350.

The corporation involved here had a capitalization of $30,000. There were three directors and their three salaries were attacked by a minority stockholder. The total of these three salaries was originally and had for years been $6,750. The three directors, all participating in the action, raised this total for their own benefit to $24,000. For the year prior to this action on their part, the corpo-

ration had earned approximately $6,000 and during the year succeeding sustained a loss of about $1,000. In the excerpt from the opinion quoted by appellant it appears "that they had voted themselves salaries by a resolution in which they all joined." At another point in the opinion the Court says:

> "They met *and voted themselves* this large increase in salary by a single resolution in which they all concurred." (Italics ours.)

The distinction between the *Davids case* and the case at bar, of course, is that in the *Davids case* the beneficiaries of the resolution themselves voted for it. As has previously been pointed out, the courts very generally condemn conduct of this kind where the recipient of the compensation, being a director himself, participates in the action of the board. This factor is not present in the case at bar which entirely distinguishes the two cases and renders the *Davids case* wholly inapplicable to the present situation.

Next is cited

Schall v. Althaus, 203 N. Y. Supp. 36.

In this case the compensation attacked consisted of bonuses given at the end of the year for which the compensation, by way of salaries, had already been fixed. It also appears that each of the officers who was also a director participated in the vote for his own salary and bonus and the Court further says:

> "It does not appear, however, that there was any substantial increase in the duties and responsibilities of the defendants."

In the *Schall case* therefore the distinguishing factors of the *Davids case* are also present and in addition, as will subsequently appear, in the case at bar the compensation awarded to the individual defendants did take into ac-

count extremely important and valuable increases in the duties and responsibilities of the individual defendants and the considerations moving from them to the corporation.

Appellant next cites the case of

Carr v. Kimbail, 139 N. Y. Supp. 253.

In that case the corporation again had three directors, one of whom was a relative of the defendant Kimball who the Court found controlled and dominated the corporation and owned a majority of the stock therein, excepting for five shares which he gave to his relative and five additional shares which he gave to the third director. All of the three directors participated in the vote increasing their own salaries.

Certain other equities favoring the plaintiff in the case were that he had formerly been a principal officer, that he had invented and developed certain lines which constituted approximately fifty per cent of the corporation's business, that he had been ousted from his official position and employment by the corporation by the defendant Kimball and the other two directors whom Kimball dominated, pursuant to a prior threat that this would be done unless he consented to an increase in Kimball's salary and that there were no increases in the duties or responsibilities of the officer directors who received the increased compensation complained of.

Appellant next cites

Ross v. Quinnesec Iron Mining Co., *227* Fed. 337.

This case involved a very complicated state of facts and was a suit by a minority stockholder seeking relief against the payment by defendant corporation to the firm of Corrigan, McKinney & Co., of commissions upon the sales of products produced by subsidiaries of the defendant corporation. The Court finds from the evidence that Corri-

gan, McKinney & Co. controlled the board of directors of defendant corporation as well as their own "and thus in effect were on both sides of the contract." This fact plaintiff, no doubt, proved by a preponderance of the evidence. The Court merely holds that when a situation such as this appears the burden is cast upon the defendant directors of both corporations to establish that the contract was a fair and reasonable one. In other words the defendant directors themselves participated, presumptively for their own benefit. in their official action as directors of both the corporations, which is not the situation in the case at bar as has been pointed out.

Church v. Harnit, 35 Fed. (2d) 499

next cited by appellant is a case of the same general character and involved the validity of bonuses given to employee-officers of a corporation who were also directors. The method of allowing and paying these bonuses was peculiar. At a meeting of the board consisting of five members, a bonus was voted to the President Harnit by the other four directors, he himself not voting. Thereafter, and when this amount had been placed to his credit on the books of the corporation he himself would divide it up as he saw fit and out of it pay bonuses to certain of the others. In other words, the directors who voted the bonus to Harnit in the first place were, in fact, voting a bonus to themselves since it was understood in advance that Harnit would pay portions of the bonus voted to him to them and, under these circumstances, the Court holds that the burden was upon the directors voting for the bonuses which they eventually received to show that they were fair and reasonable. [See Appendix p. 18.]

In the lower court the plaintiff's bill was dismissed and this was affirmed on appeal, it being found that the com-

pensation was fair and reasonable This is simply another of many cases which hold that where a director does himself participate in the vote affording him increased compensation without a corresponding increase in his duties and responsibilities, the burden is cast upon him to establish his fair dealing, which is not at all the case at bar.

The next case cited is

Jordan v. Jordan (Conn.), 109 Atl. 181.

In this case no question of salary was involved. The corporation required additional funds as capital because of increased business and sought to obtain them from one Sisk who was elected a director of the corporation. The suit involves an investigation of the financial transactions between Sisk and the company. Sisk would discount accounts and receivables of the corporation for cash. The claim was, in effect, that the discount he received for doing this and the profits he personally made in selling certain property of the corporation were excessive and unconscionable. A mere reading of the facts would seem to demonstrate that this was true. While the trial court found that the burden was on the company's receiver to prove fraud, the Appellate Court very properly holds otherwise.

The situation on the face of things showed the realization of large profits by Sisk on each of the transactions complained of which alone gives rise to a presumption that the property which he obtained from the corporation and resold was worth appreciably more than the price at which he obtained it from the corporation. This is obviously a very different situation from the one with which we are concerned.

O'Leary v. Seemann (Colo.), 232 Pac. 667

next cited, was a suit for an accounting by stockholders against the president of a corporation who had taken from the corporation a commission of twenty-five per cent for selling corporate stock. Such a commission or any commission to the defendant president had never even been authorized by a meeting of the board of directors. The Court considers whether the president may be entitled to keep what he has been paid on a *quantum meruit,* entirely aside from any authorization by the board. [See Appendix p. 18.]

The Appellate Court granted a new trial.

The last case cited by appellant on this point is

Davis v. Thomas A. Davis Co. (N. J.), 52 Atl. 717.

The suit is one by stockholders to compel three directors and officers of defendant corporation to return "all or a portion of the salaries which these three directors *voted to themselves.*" (Italics ours.) There were three directors and it clearly appears that they all participated in the vote of the board which resulted in the salaries complained of. Here again is a case, of which there are many, which lays down the rule that where the beneficiary of the vote participates in the voting, the courts will scrutinize the action of the board and the burden is shifted to the participating director to establish the fairness of the board's action. With this principle we have no quarrel but as repeatedly stated it is not applicable to the facts in the case at bar. We submit, and are confident that a careful analysis of the cases cited by appellant on the question of burden of proof will support the position of respondents where the facts are at all applicable, that such of the authorities as cast the burden upon the defendant are based upon facts not present in our case

which totally distinguish them. Many of the cases cited by appellant in support of its position are from the Appellate Division of the New York Supreme Court. The most recent case on the subject from that Court appears to be

Heller v. Boylan (1941), 29 N. Y. Supp. 651

which was an action by minority stockholders to recover "for the corporation from the company's directors for alleged improper payments to certain of the company's officers." Syllabus 6 of the headnotes reads:

> "In stockholders' derivative action to recover for corporation from corporation's directors for alleged improper payments to certain of its corporate officers on theory of waste, the burden of proof was on plaintiff stockholders."

Citing

Seitz v. Union Brass and Metal Mfg. Co. (Minn.), 189 N. W. 586.

We have heretofore cited and quoted from numerous decisions of the New York Supreme Court and Court of Appeals which definitely establish the rule in that state, in cases where the facts are as they are here, to be in accordance with respondents' position.

We therefore submit that the power of this Court to review the facts, and the findings of fact made thereon in the court below, are subject to the limitation of the rule applicable to actions at law and that, whether the action be regarded as one in equity or at law, the burden of proof is upon the plaintiff to establish by a preponderance of the evidence both the fraud and the excessive compensation alleged.

An Analysis of the Proof Produced by the Respective Parties.

Assuming it to be established that the burden of proof is upon plaintiff to prove, first, a fraudulent conspiracy, and second, the payment of excessive salaries as the result thereof and, assuming further that on this appeal the findings of fact of the lower court will not be disturbed if supported by evidence and unless clearly erroneous, an analysis of the testimony and the record on these two points is necessary.

In the first paragraph of its argument on page 22 of its brief, appellant makes numerous misstatements of fact as a mere reference to the record pages will demonstrate and the untruth of some of which has already been pointed out.

Appellant offered no testimony on the issue of fraud and conspiracy. Proof is wholly lacking on that issue.

The only evidence offered by plaintiff on the issue of excessive compensation which even tends to support its claims in that regard are the tabulation of its witness Bunch [Pl. Ex. 15, R. 438] printed at page 27 of its brief and the opinions and conclusions of plaintiff's president, Dulin [R. 387-417]. Bunch had been an "analyst and statistician," a stockbroker and "investment counsel," a "financial writer" and "public relation counsel" [R. 418]. His examination on *voir dire* [R. 419 *et seq.*] should certainly demonstrate his lack of competency as a witness on this issue. An objection to his testimony was overruled [R. 422]. Plaintiff's Exhibit 15 which he had prepared was admitted without objection [R. 436] though it is obviously the rankest kind of hearsay and incompetent on innumerable grounds. There is nothing whatever to show any reasonable comparison between the business of defendant corporation and any of the concerns listed in the exhibit nor between the particular exigencies confronting these concerns, if any, and the very decided crisis and necessity for developing new products and an increased volume facing the defendant. Neither is there anything to show, nor was there any opportunity to cross-examine, concerning the number of executive employees

working for the concerns listed on the exhibit in addition to those receiving the "two highest salaries" or the nature and extent of the work of such other employees supplementing that of the recipients of the two highest salaries. The merest consideration of this exhibit at once demonstrates its inadmissibility as evidence, but even more, its total lack of any probative value in establishing the contentions of plaintiff. Most of the cases which have passed upon the subject have held both, that what may be paid employes in some other business than the one under consideration, and also, what the individual has earned or might earn in some other employment, are immaterial in cases of this kind. The sole question is, *what are the services of the individual whose compensation is questioned actually worth to the corporation by which he is employed.*

> *Fletcher Cyc. Corporations,* Perm. Ed. Vol. 5, Sec. 2180, p. 501 and cases there cited.

We submit, without wasting any more space on it, that Exhibit 15 contains no evidence worthy of consideration.

As to Dulin's testimony on the issue of whether the salaries complained of are reasonable or not, he admits that he favored an increase in the salaries of Messrs. Patterson and Ballagh made by the board in October, 1938, from $1,000 to $1,500 per month each [R. 388-389], and also the increase in Mr. Miller's salary from $1,000 to $1,500 per month voted at a meeting in March, 1940 [R. 389]. Mr. Dulin's testimony may be searched in vain for anything whatever going to the issue of whether the compensation paid to defendants *is reasonable.* In fact there is nothing on the question in any part of his testimony excepting reference to his having voted against certain increases and having objected thereto, all of which, naturally, proves nothing.

Appellant's only other witnesses were called in rebuttal solely for the purpose of giving their opinions of the value of the various inventions developed by the defendant officers, the rights in which the latter assigned to the corporation [R. 510, 514, 520, 527, 530.]

The first of these was the witness Grant [R. 542-550]. He was a purchasing agent employed by a well-drilling contractor, with very limited experience and practically none in any oil producing area other than California [R. 549]. He had had no experience with the lip protector or any of the other inventions devised by defendant officers [R. 548] and without consuming further space we submit that his testimony has neither probative value in support of appellant's case nor anything to rebut the case of respondents for which sole purpose it was produced.

Appellant's only other witness is one Chestnut [R. 565-579], an employee of appellant who was also called to rebut respondents' testimony relative to the value of the inventions devised by respondents for the corporation. Here again a reading of the entire testimony demonstrates conclusively that it proved nothing whatever affirmatively to support appellant's allegations of fraud, wrongdoing and excessive salaries and has little or no value in rebutting respondents' case as to the value to defendant corporation's business of the inventions designed by Messrs. Ballagh and Miller for which sole purpose it was produced.

We therefore have a case where plaintiff alleges fraud. conspiracy and tortious conduct as the result of which the individual defendants procured excessive salaries to be paid to themselves. As for testimony to establish these charges plaintiff offers absolutely nothing whatever on the issue of conspiracy, fraud and tortious conduct and nothing on the question of reasonable compensation other than the incompetent Bunch exhibit [App. Ex. 15], and Dulin's testimony relative to certain objections which he made to some but not all of the increases complained of.

No wonder appellant argues that the law only requires the filing of a complaint to prove its case. It literally has nothing else. On this state of the record alone the presumptions favoring defendants compel a decision in their favor.

Respondents, however, prove their case by evidence. Their oral testimony was that of Messrs. Ballagh, Miller, and Burrell, all directors, and Mr. Morris, an employee.

Mr. Ballagh, the real originator of the business, gives a history of his own background, the commencement of the business which later resulted in the incorporation of the company, and of the latter's business from the time of its incorporation [R. 472-542]. The business first consisted of the manufacture and sale of so-called pipe line protectors made of rubber, the purpose of which he describes [R. 475]. This device was patented by one Bettis with whom a licensing agreement was made in 1927 [R. 476]. In 1929 the sales of this item were $1,111,000. In 1930 they were $636,000. In 1932 they dropped to $149,000 and in that year the Bettis patent was declared invalid by the U. S. District Court [R. 478], as the result of which some sixty competitors commenced marketing the same or a similar product [R. 479]. This situation necessitated the development of other or "non-protector" items for sale, the first of which was marketed in 1936 (retread rubber and not invented articles) [R. 479]. Mr. Ballagh devoted practically all of his time during daylight hours from the latter part of 1938, to the work of the corporation and spent at least three nights a week at home working on various inventions and other sales work for the company. He acted as sales manager and had charge of the advertising [R. 483] and in addition handled certain important patent litigation both in Oklahoma and California [R. 484]. He took no vacations [R. 483]. As the result of this Ballagh devised a number of new articles for manufacture and sale, among which were the lip protector, the nature and purpose of which he describes [R. 510-514], the Hydraulic applicator [Defendants' Exhibit J, R. 489-505], the sucker rod protector [R. 487, 521, 528], the pipeline wiper [R. 489, 514, 518, Defendants' Exhibit M], the Kelly wiper [R. 519, 521] and a plastic tubing protector [R. 523, 530]. The nature, purpose of and gross profits on all of these items are described much better by Mr. Ballagh in his oral testimony than we can attempt to describe them here. We should point out, however, that the lip protector is an improvement on the invalidated Bettis protector, the nature of which Mr. Ballagh describes, and on which the company has no competition [R. 510-514] and that the Hydraulic applicator affords an im-

proved means for installing protectors on the pipe which further reduces competition on protectors generally and has resulted in acquiring for the company many new customers in the mid-continent field and in California, among which are the Associated Oil Company, The Shell Company, the Union Oil Company, the Barnsdall Company, the Richfield Oil Company, Bellridge Oil Company and the Texas Company [R. 505]. All of these devices were developed and placed on the market from about the beginning of 1939 [R. 401] and during the three-year period here involved. Each of them has more than doubled in sales in each successive year as is graphically shown by the chart [Defts. Ex. G, reproduced in the Appendix, p. 53]. The actual sales figures year by year are given in Mr. Ballagh's testimony [R. 487-488], which, however, do not reflect the value of the Hydraulic applicator and lip protector inventions, the effect of which is to eliminate competition on and increase protector sales formerly protected by the invalidated Bettis patent.

Miller became president on February 15, 1939, and, in addition to performing his duties as such, managed the factory, attended to the finances, purchasing and did certain inventing. Up to the time of the trial he had invented the steel-clad open hole stabilizer, the steel-clad protector, the rod protector [R. 373], a rod wiper and two line wipers [R. 374]. The progressive sales by years on these items are shown in the chart [Defts. Ex. A. and the figures in dollars and cents are given in Miller's oral testimony [R. 376-377].

The testimony of Mr. Morris, [R. 459-472] who was a salesman in the defendants' employ in the mid-continent field, describes the use of the various devices developed by defendants Ballagh and Miller, their practical elimination of competition in the territory with which he was familiar and their effect upon the sales volume of the company.

Mr. Burrell [R. 428-446] gives as his reasons for approving Mr. Ballagh's compensation, the great amount of time and effort devoted by him to the company's sales, the important part he played in patent litigation in Oklahoma [R. 435], the perfection by him of the Hydraulic appli-

cator "which I consider the most important thing that had as yet been received by the company in the last few years" [R. 431], "a great many activities outside the ordinary course of his duties in developing articles and devices" [R. 433], the development of the lip protector [R. 435] and the development of the pipe wiper [R. 440]. As to his reasons for voting for Mr. Miller's compensation, he testifies that Miller, being in charge of the finances, the operations of the factory and the purchasing of supplies had caused an improvement in the financial condition of the company, that the ratio of assets to liabilities was improved, that he had installed various efficiencies in the plant and office [R. 433], that he was engaged in the development of certain new products and that Mr. Dulin had no objection to the increase [R. 434]. As to the compensation to both Messrs. Ballagh and Miller in so far as the matter of inventions was a factor, it was Mr. Burrell's opinion that the inventions belonged to the inventors in the absence of assignments or licensing agreements. He testifies that they either had been or would be transferred as soon as invented or as soon as patents were applied for [R. 449] and that it was distinctly to the company's advantage to compensate Ballagh and Miller for the use of these inventions on a salary basis which was flexible from time to time depending upon the general condition of the business, rather than to definitely obligate the company to pay royalties under licensing agreements [R. 450-451]. Each of the inventions of Messrs. Ballagh and Miller and all rights therein including the patent rights already acquired and those applied for, were assigned by the inventor to the corporation and the corporation has manufactured and sold the items from the time of their invention royalty free. On this there is no dispute [R. 510, 514, 520, 527, 530].

Appellant claims, however, to have proven that respondents' compensation was excessive: that the compensation cannot be justified by respondents' claimed services as inventors, and that respondents' compensation was arranged as a part of a conspiracy between them to fraudulently enrich themselves at the expense of appellant and minority stockholders (appellant being the only one (App. Br. 48-52) under certain specific headings.

We will discuss each of these contentions in the order and under the headings in which they appear in appellant's brief:

"(a) *It* (the compensation) *was in excess of salaries paid by comparable but larger companies.*"

This whole argument is based on the Bunch exhibit [Pl. Ex. 15]. We believe what has heretofore been said should dispose of this exhibit as evidence. The argument is further vulnerable because of the evidentiary principle that what other employers pay to other employees is wholly immaterial, the only material question being what were the services of these defendants worth to the defendant corporation.

"(b) *The salaries paid to the defendants were several times greater than their prior compensation had been from other companies by which they had been employed.*" (App. Br. 28.)

In the first place what respondents have been paid in previous employments was wholly immaterial and inadmissible.

> *Fletcher's Cyc. Corp.*, Perm. Ed., Vol. 5, Sec. 2180, p. 501 and cases there cited.

The testimony was particularly objectionable as to the defendant Ballagh who, in reality, founded the defendant corporation's business in 1927 and has been employed by no one else than the defendant corporation and its predecessor partnership in the interval of approximately fifteen years. Obviously, the compensation which he may have received in any employment more than fifteen years previously was too remote to merit consideration, assuming it were admissible otherwise, nor was any comparison whatever sought in his examination relative to the duties in his previous employment as contrasted with those performed for defendant corporation.

Mr. Miller's employment elsewhere was more recent than Mr. Ballagh's. His examination on this point was objected to and erroneously overruled provisionally. The trial court never did finally pass on the admissibility of

the testimony (App. Br. 379). Here again nothing was elicited to permit a comparison between the value of the services rendered in some other employment and those rendered to defendant corporation.

We submit that appellant's argument under this heading is not worthy of any consideration by this Court.

"(c) *The salaries paid to the defendants were out of all proportion to the net profits of the corporation.*"

This, as are all the other arguments of respondent on the question of the reasonableness of defendants' compensation, is based largely on the incompetent and non-probative Bunch report [Pl. Ex. 15]. During 1939, 1940 and 1941, the years under consideration here, the management of the company was endeavoring to develop articles for manufacture and sale to take the place of the Bettis protector, the patent on which had theretofore been invalidated. This could only be done by developing new devices for use and sale in the general field of defendant company's activities, that is the field of oil well supplies, and this could best be done by inventing such new articles and devices. At this time it was not so much a question of current net profits but rather of investing time and money in developing additional products for the future. The determination of that policy was purely one within the discretionary powers of the Board of Directors of the company and the circumstances would, under all the decided cases, be very exceptional where a court would be justified in reversing or interfering with a policy of that kind determined by a corporate Board of Directors within the sphere of its proper jurisdiction. However, this policy as determined upon and carried out during the period resulting as it did in conferring upon the corporation a variety of new articles with which to supplement its line, did not decrease the company's earnings nor deplete its reserves. On the contrary its sales and earnings steadily increased during the period in question. [Pl. Ex. 4, R. 291.]

The consistent improvement in the earnings and financial condition of the company during the years 1939, 1940

and 1941 are reflected in the so-called Pennington audits [Pl. Exs. 5-A, p. 1, 5-B, p. 1 and 5-C, p. 2] as follows:

Net worth, end of year 1939	$243,598.42	
Net worth, end of year 1938	222,671.17	
Net gain for 1939		20,927.25
Net worth, end of year 1940	264,118.27	
Net worth, end of year 1939	243,598.42	
Net gain for year 1940		20,519.85
Net worth, end of year 1941	201,023.44	
Net worth, end of year 1940	181,802.80	
Net gain for year 1941		19,220,64

During these years the compensation to defendants complained of was being paid and, in addition to the net gains above shown for each year, an additional surplus for the period of $22,649.23 was accumulated to meet certain contingencies and particularly the contingent liability arising out of the suit brought by plaintiff for royalties on the invalidated Bettis patent which is now pending in this Court [R. 362]. These net gains for each of the three years remain after providing for all tax and other contingent liabilities including depreciation, as the audits will show. This means that at the end of the year 1939 the corporate stock had a book value of 243% plus, at the end of 1940, 264% plus and at the end of 1941 201% plus, based on a par value of $100 per share. The reason for the decrease in the book value between the end of 1940 and 1941 was the comparatively large amount set aside in the contingent reserve account in the interim and the elimination of $80,703.61 for goodwill as an asset. It will also be observed that during the three years the company earned, in 1939 $20.93 a share, in 1940 $20.52 per share and in 1941 $19.22 per share, all on a par value of $100 per share, which we submit is somewhat conclusive evidence of good management and the formulation of good business policy on the part of the company's

directors during this trying period. If these figures are compared with the profit and loss and capital and surplus figures shown on the Bunch exhibit [Pl. Ex. 15], the advantage is all with the defendant corporation. It is interesting to note that at the end of the three years in question there was available for distribution as dividends to the stockholders the following:

1939	$143,598.42
1940	164,118.27
1941	101,023.44

and, in addition thereto, there had been accumulated the reserve account above referred to by the end of 1941 and the item of goodwill theretofore carried as an asset in the sum of $80,703.61 was eliminated, notwithstanding which at the end of the year 1941 the stock still had a book value of $201 per share plus, as against the par value of $100 per share, and there remained $101,023.44 available for dividends. The fragmentary figures contained in appellant's brief at pages 29, 30 under this heading which are, for the most part, random monthly operating results for only *such* months as best suit appellant's purposes, are wholly misleading and do not give a fair representation of what the situation actually was.

Appellant concludes its argument under this heading by another reference to the Bunch figures [Pl. Ex. 15], which, it says, present no comparable cases except those where the particular company shown in the exhibit was either operating at a loss or "*had several times* more capital and surplus invested." The Court is probably sufficiently familiar with the general nature of most of the businesses listed in the exhibit to realize that most of them are engaged in heavy industry producing what are known as durable goods, a basic characteristic whereof is the investment of large amounts of capital producing comparatively small profits, and whose products sell on

very narrow margins of profit. The business of defendant corporation is not of this type at all. It produces highly specialized articles selling at a very high rate of gross profit. Its heart and life blood have little relation to the capital invested but are the development of efficient and non-competitive items in the field of oil well supplies. This could only be accomplished by invention and great activity in efficient marketing and, therefore, the success or failure of the business depends directly upon the accomplishments and activity of the individuals responsible for its operation rather than on its invested capital. These individuals were the individual defendants.

We believe this should effectually dispose of appellant's argument under this sub-heading.

"(d) *The salaries paid to the defendants were out of all proportion to the invested capital and the size of the business of the corporation* (App. Br. 31).

Appellant's argument under this heading has perhaps been sufficiently answered in respondents' reply under the last heading. Here again, the appellant's sole reliance is the wholly incompetent, irrelevant Bunch exhibit [Pl. Ex. 15], which, without a proper foundation to afford a comparison between the businesses listed thereon and that of defendant corporation or the services rendered for the "two highest salaries" and those rendered by defendant is quite without probative value. We desire to point out, however, that, even on the basis of the Bunch exhibit, defendant corporation's ratio of profit to capital and surplus even after paying the compensation complained of, accumulating a reserve against the contingent liability of the Byron Jackson Co. royalty suit and charging off the very large item of goodwill heretofore referred to, is approximately 11.5 per cent, which ranks eleventh in the list of the thirty-five businesses listed in the exhibit. We repeat, because it is an important factor in determining

the reasonableness of the compensations complained of in this case, that defendant corporation's business is one in which the size of the invested capital is a matter of comparative unimportance. The investment in an executive sufficiently expert, capable, resourceful and having the qualifications essential to developing and marketing essential products in the company's chosen field of operation is very much more important than is the investment of a large amount of money in heavy machinery which will produce tile and similar clay products, steel and metal articles or pulp and paper such as is being done by such concerns as Gladding McBean & Company, Western Pipe & Steel Company, Consolidated Steel Corporation and Puget Sound Pulp and Timber Company, to mention a few listed on the Bunch exhibit.

"(e) *The increases in defendants' salaries were made without any corresponding increase in the amount of the responsibility of the services rendered or to be rendered by defendants.*

We have already pointed out that prior to the invalidation of the Bettis patent and from the inception of the defendant company's business, the principal item which it sold was pipe line protectors licensed, and presumably protected, by the Bettis patent. In 1929 these sales amounted to $1,111,000. In 1930 this figure had dropped to $636,000 and in 1932 to $149,000. That was the year in which the Bettis patent was invalidated by the District Court [R. 478]. To make up for this drastic reduction in the sale of its article the company went into the business of making retread rubber, a staple, nonprotected, highly competitive article. It was realized, however, that other articles more closely related to the field of oil well supplies would have to be developed if the company were to survive [R. 479], and consequently Mr. Ballagh, as well as Mr. Miller as soon as he became connected with

the company, both of them experts in the field, turned their attention to the invention and development of such items but none of them was invented or developed prior to 1938 [R. 509].

Even Bunch had no information as to whether the executives receiving the "two highest salaries" in his exhibit "ever invented devices and gave them to the corporation royalty free" [R. 419]. He knew nothing whatever about the business of defendant corporation "except its financial data and the salaries that the officers draw and the general facts of its financial setup and operation." He didn't know anything about hydraulic applicators [R. 420] nor about the importance of protectors or pipe wipers [R. 421]. But he did know that patents and inventive rights in the oil business have a "very high value" [R. 423] and that businesses which have enjoyed very prosperous years have proceeded to lose money and lose their business to competitors due to some betterment of the article of their competitors [R. 424]. Incidentally, during the years when the business was depressed owing to the invalidation of the Bettis patent and between 1931 and 1939, there was paid a total of $30,418.42 to the plaintiff in dividends and royalties the greater part of which ($27,418.42) was for royalties on the invalidated patent [Pl. Ex. 18-D]. In support of its argument under this heading appellant cites certain cases each of which is readily distinguishable from the case at bar (App. Br. 33):

Schall v. Althaus, 203 N. Y. S. 36,

already commented on, involved bonuses given at the end of the year for which the salaries to be paid were already fixed and determined and were consequently mere gratuities. Also in each case the recipient director voted for his own salary and bonus and the court says:

> "It does not appear however that there was any substantial increase in the duties and responsibilities of the defendants."

which was most certainly not the situation in the case at bar.

Atwater v. Elkhorn Valley Land Co., 171 N. Y. S. 552,

next cited was about as different in its facts from the case at bar as could well be imagined. The corporation owned coal lands in West Virginia which it leased on royalty. There was nothing whatever to do but distribute the proceeds from the royalties. All the work was done by a $100 per month clerk. One Andrews was the president, Jones, his son-in-law, and Lee, the secretary, likewise a relative, were the directors. The latter two had been given their small amounts of stock by Andrews. On appeal, the secretary's salary was the only item involved. It appeared that he was a city employee working as such every day from nine in the morning until five in the afternoon; then he went to the company's office two nights a week; attended monthly directors' meetings and kept a rough draft of their minutes. There was no change of any kind in his duties or responsibilities.

Kreitner v. Burgweger, 160 N. Y. S. 256,

was obviously a very aggravated case from the standpoint of minority stockholders. The corporation had a capital of $250,000 and an accumulated surplus of $700,000 and had never paid more than four per cent in dividends notwithstanding the disproportionate surplus. There were three directors, directors representing the minority stockholders having been dropped from the board. All information relative to the affairs of the corporation was denied to the minority stockholders and could only be obtained by mandamus which had, on occasion, been done. $30,000 of the company's funds had been withdrawn by the officers and not accounted for. Political contributions and donations of various kinds had been made without authority

and there were no circumstances which could invoke the *quantum meruit* rule which will be later discussed. There were no increases whatever in the duties or responsibilities of the beneficiary directors and officers.

The last case cited by appellant under this sub-heading is

> *Raynolds v. Diamond Mills Paper Co.* (N. J.), 60 Atl. 941,

from which a short and misleading excerpt is quoted. The first purpose of the suit was to compel the declaration of a dividend and it was, consequently, one seeking relief in the nature of a mandatory injunction and therefore equitable in character. The second purpose was to compel the return by directors and officers "who had fixed their own salaries and drawn the amount of these salaries from the treasury of the corporation," whatever the court might find to be excessive. It is interesting to note the following comment of the court:

> "Now, we have these two, as it seems to me, radically different causes of action combined in one bill. No objection has been made to the joinder of these two causes of action."

Clearly implying that the first is equitable and the second legal in its character. The capital stock of the corporation was $300,000 and it had assets of a value between $500,000 and $600,000, had made large profits for the several preceding years and with these had steadily extended its business, acquiring more mills and machinery. However, the Court on the issue of dividends, decides the case in favor of the defendant. [See Appendix p. 19.] As to the salary issue this case differs from that at bar in the fundamental, which seems true of all the cases cited by appellant, that the compensation complained of was, in each case, determined by the affirmative vote of the beneficiary himself. [See Appendix pp. 19-20.]

The Defendants' Services Other Than Those Prescribed by the By-Laws.

Appellant prefaces its argument under its main title "3" commencing on page 34 of its brief, with a most unusual complaint. It dwells upon the "injustice" of permitting defendants to urge the value of their services rendered to the corporation for devising and inventing articles of manufacture and sale because, forsooth, "not one word was said about inventions or patents in plaintiff's complaint." After all, the defendants didn't draw the complaint. Appellant then bewails the fact that there was "no word of inventions or patents" contained in the answer and therefore "in all fairness" defendants' services in that connection "should not have been considered by the Court." It is difficult to imagine a more puerile wail than this. Plaintiff alleged that the defendants had been excessively paid. Defendants denied that allegation and naturally had a right to open up the entire field to show the exact nature and value of the services which they rendered the corporation for the compensation which it paid them.

"(a) *The by-laws of the corporation and the resolutions passed by its board of directors showed that the defendants were not being compensated as inventors."*

Reference is first made to the by-laws of the corporation and the offices created thereby. The by-laws do not create any offices at all excepting those of *president, vice-president, secretary* and *treasurer*. [See Appendix p. 20.] The duties of the president as prescribed by the by-laws do not, no doubt owing to some oversight, appear in the record. The court, however, is familiar with the usual stereotyped provisions, customary in corporate by-laws, defining the duties of corporation presidents, which are usually confined to mere formal corporate acts, and it can, no doubt, properly take notice that the by-laws of the

defendant corporation do not differ from what is ordinarily the case in this regard. The duties of the secretary-treasurer were read into the record as a part of the testimony of defendant Ballagh [R. 485-486] and are of the stereotyped formal corporate character referred to. They include nothing relating to the management or promotion of sales, the development or invention of articles of manufacture and sale nor any other duties relating to the actual and productive purposes and aspects of the business.

At the annual directors' meeting of February 15, 1939, (206 *et seq.*), [Pl. Ex. No. 1] the following appears:

> "The meeting then proceeded with the matter of considering the compensation to be paid the president for his services and *the advisability of designating him as General Manager of the business and affairs of the corporation.*" (Italics ours.)

and a resolution was introduced and passed, *with the seconding by and the vote of Director Dulin,* appellant's president, that Mr. Miller be designated General Manager in addition to president. At a special meeting of the Board held on March 18, 1940 [R. 240, *et seq.,* Pl. Ex. 1], as to defendant Ballagh, it was "pointed out that his services in addition to those of said office (secretary-treasurer) *also include those of a sales manager,* in view of the fact that Director Ballagh was and had been for many years in complete charge of all sales activities of the corporation. The statement was made that during the last few months there "had been a sharp increase in the volume of sales and that the efforts devoted to the business of the corporation by Director Ballagh had been showing very satisfactory results." It therefore conclusively appears that the duties and responsibilities of defendant Miller were increased at the beginning of the

year 1939, which increase continued during all of the three years here in question, from those merely of president of the corporation as defined in the by-laws, to those of General Manager and that the duties of Mr. Ballagh were increased officially in March of 1940 from the formal duties prescribed for the secretary and treasurer in the by-laws to those of Sales Manager and further that it was officially recognized that he had been discharging the latter duties since at least the beginning of 1939 even though the official recognition of the increase in his duties did not occur until March of 1940. From a technical standpoint therefore, it clearly appears that the duties and responsibilities of both defendants were increased.

Technicalities aside and getting into the real merits and substance of the matter their actual duties and responsibilities as well as the value of the services rendered by each of them to the corporation, were tremendously increased by the invention and development of all of the various new articles of manufacture and sale which are enumerated and described in the record and which we will not take the space to re-enumerate.

To support its position under this heading the appellant first cites the case of

Stratis v. Andreson (Mass.), 150 N. E. 832.

We confess we do not see the point of the citation from appellant's standpoint. It appears to us that on this particular issue, as well as on others in connection with which we have previously analyzed the case, it is strong authority for the position of respondents. One of the defendants in that case whose compensation was complained of was employed as "treasurer, general manager and clerk" of the defendant corporation and he was paid separate salaries for each of these position "in the amounts of $6,000, $6,000 and $2,500 respectively, or $14,500 in

the aggregate." The facts in the case were referred to a special master who found that the compensation paid to this individual as a clerk was excessive and, therefore, the excess over the reasonable value of his services in that capacity should be returned by him to the corporation. The quotation from the case appearing at page 36 of appellant's brief is sufficient to dispose of appellant's point. If the individual defendants at bar had been paid *separate compensations* in their separate capacities as president, general manager and inventor in the case of Miller, or secretary-treasurer, sales manager and inventor in the case of Ballagh, it would, under the authority of the *Stratis* case be proper, if any competent proof were adduced by plaintiff to show that the compensation in any category was excessive, to inquire into that question. However, in the case at bar no separate compensation was paid to either Messrs. Miller or Ballagh for the different types and kinds of services they rendered to defendant. To use the language of the Massachusetts Court, their entire compensation was paid as a "unit" instead of being split up as it was in the *Stratis* case and, therefore, if "the entire compensation regarded as a unit was not excessive" and plaintiff has not sustained any burden of proof nor offered any competent proof at all that it was, its case must fall. Obviously on the point under consideration the *Stratis* case is no authority for appellant's position. Quite the contrary.

Appellant next cites

> *Lillard v. Oil Paint & Drug Co.* (N. J.), 56 Atl. 254,

from which case a long quotation appears at page 37 of appellant's brief. The case involves a complicated statement of fact and corporate history and, because of the variety of relief sought, it was obviously equitable in

character. The sole issue of which the Court took any cognizance and for which it granted any relief finally boiled down to the reasonableness of a salary and the gist of it appears at page 260, quoted in the Appendix, p. 20. Incidentally, this is one of many cases holding that what one may have been paid in some other occupation or might earn in another employment is wholly immaterial to the question under consideration, the sole question being what are the services worth *in the particular employment under investigation.* In the *Lillard* case the Court specifically says that there have been no increases in either the duties or responsibilities for which the compensation was paid.

At page 38 of its brief, appellant seeks to twist an assertion in respondents' memorandum brief in the trial court into an admission that all respondents were entitled to be compensated for were the stereotyped formal services prescribed in the by-laws for the official corporate positions to which they had been elected. Whatever may have been said in the memorandum brief in the trial court is, of course, immaterial here, but what was there said contrasted cases where employees are endeavoring to recover compensation from a corporation, many of which were cited by appellant in the trial court, and cases such as this where a minority stockholder is seeking to recover back for the corporation compensation already paid by it to an employee. Obviously there is a great distinction. Respondents have never "conceded," nor do they now, that they "must look to the resolutions of the Board of Directors for such compensation as they received." They do contend, however, that they are entitled to compensation for their services as president, General Manager and for the development of inventions and devices so far as Miller is concerned, and as secretary-treasurer, Sales Manager and the development of devices and inventions so

far as Ballagh is concerned, paid in each case as a unit and not split up into separate categories as in the *Stratis* case, *supra,* and furthermore, as will later appear, that their services as General Manager and Sales Manager respectively, which are nowhere defined in the by-laws, resolutions or elsewhere were comprehended and understood by all of the stockholders and directors to include the development of devices and inventions for which they were to be compensated. As to these latter services, respondents claim they are entitled to compensation by reason of the well defined general understanding by the directors of the duties which were to be performed by them as General Manager and Sales Manager respectively, and in any event upon the *quantum meruit* theory.

"(b) *The services as inventors, for which the defendants claim compensation, were never performed for the corporation.*"

We are wholly at a loss to understand appellant's argument under this heading. Reference is first made to page 40 of respondents' trial memorandum from which a short quotation appears. Respondents' entire argument from which this quotation is excerpted, was to the effect that if the devices and inventions developed by the defendants had not been compensated for by the corporation by way of salary or otherwise as they were, and in the absence of their assignment by the inventor in each case to the corporation, they had been developed under circumstances which would constitute them the property of the inventor, all for the purpose of showing that for the compensation paid by the corporation to the inventors, the corporation gained great value which it otherwise would not have received and owned. Inasmuch as counsel has seen fit to quote a short excerpt from the argument presented in the trial court which

is obviously misleading, we quote the argument from which it was excerpted, in the appendix. [Appendix p. 20.]

Appellant next quotes excerpts from the testimony of Messrs. Ballagh, Dulin and Burrell, the obvious meaning of which is merely that, in the absence of compensation paid to Ballagh and Miller for their inventions and an assignment or an agreement to assign to the corporation, these inventions would have remained the property of the individual inventors. The fact, however, is, as has already been pointed out with appropriate reference to the record, that as the result of the common understanding between all the directors and parties interested, both Ballagh and Miller undertook their experimental work for the benefit of the corporation [R. 170, 186, 189, 194, 202] expecting to be paid therefor as they were by increased salary compensation [R. 382, 430-435, 440, 448-459, 564] and in every instance they assigned their patent rights, either actual or prospective, to the corporation [R. 449, 450, 527]. If under all these circumstances the inventions and devices were not developed for the corporation, it seems difficult to know for whom they were developed. After all, "the proof of the pudding is the eating thereof" and the corporation manufactured and sold all these devices and inventions from their inception royalty free, is still doing so and it owns by valid contracts of assignment in writing, all rights, patent and otherwise, present and prospective, in all of them. Appellant says that Dulin knew nothing about these inventions and cites page 406 of the Record. In the answer to the question as to whether Dulin knew about the inventive work Miller and Ballagh were doing, he says "I did not. During the period you are speaking of I was in Washington, at the request of the Government, over twenty times, and spent half of my

time outside the State of California." Under these circumstances it is obvious that Mr. Dulin was hardly in position to know much about the problems of the defendant corporation which he was supposed to be serving as a director. The minutes show, however, that experimentation and invention was discussed at numerous meetings [R. 170, 186, 189, 194, 204], and Director Burrell, a wholly disinterested party, testified that these inventions and devices were discussed "at practically every meeting" [R. 456, *et seq.*]. During the three-year period in question Dulin, even according to his own statement, spent altogether eighteen hours on the defendant corporation's business [R. 427] including "a substantial amount of time" which he says he devoted to the defendant corporation's affairs away from its premises and in his own office [R. 416]. It seems an obvious inference that Mr. Dulin was more interested in continuing to milk the defendant corporation for the benefit of Byron-Jackson & Co., of which he was the president, than he was in the welfare of the defendant corporation of which he was a director.

In concluding its argument under this sub-heading, appellant asserts that "authorities are to the effect that when an officer performs services outside of his duties he must have a contract with the corporation before he can recover for such services," and cites certain cases. If reliance is placed upon the technical corporate duties prescribed by the by-laws for the president, secretary and treasurer, we have already pointed out that both Messrs. Miller and Ballagh were appointed by the directors as General Manager and Sales Manager, whose duties are not prescribed anywhere but it was generally understood by all the directors and parties interested to comprehend and include the development of devices and inventions.

Appellant's language just quoted is neither a correct nor accurate statement of the law. The rule is stated in Fletcher on Corporations, Perm. Ed., Vol. 5, Sec. 2114, p. 387 in heavy type, as follows:

> "By the great weight of authority, if directors or other officers render unusual or extraordinary services for their company, not within the line of their ordinary duties, the circumstances may give rise to an implied promise for compensation under the general rules governing all implied contracts."

Numerous cases are cited from all the American states, as well as the Federal Courts, including the Supreme Court of the United States, to support this statement of the rule and the rule is the same in California.

In Section 2115 at page 393, it is said, quoting from *Hunter v. Conrad,* 230 N. Y. S. 202:

> "'. . . it is clear that a director of a corporation may lawfully be paid for services performed beyond the ordinary duties of a director.'"

and the section proceeds to give illustrations of such extraordinary duties. For example, where a director happens to be an attorney who performs professional services for the corporation or acted as its general counsel, or where a director acts as general manager and superintendent of construction. or used exceptional and extraordinary efforts in selling corporate stock, or performed manual labor outside of his duties as a director, or was an expert bookkeeper and auditor and furnished services of that character, or one who acts as an arbitrator in settling a dispute to which the corporation is a party, or acts as an agent or broker in procuring patents to land, or in obtaining loans, or in securing rights of way for a railroad, or acts as captain of a boat

owned by the corporation, an implied contract arises that the corporation becomes indebted to him for such services.

Taussig v. St. Louis & K. R. Co. (Mo. Sup. Ct.), 65 S. W. 936;

Fox v. Arctic Placer Min. & Mil. Co. (N. Y.), 128 N. E. 154. [See Appendix p. 23];

Jackson v. New York Central R. Co., 58 N. Y. 623;

Watts v. West Virginia Southern R. Co. (W. Va.), 37 S. E. 700;

Spence v. Sturgis Steel Go-Cart Co. (Mich.), 186 N. W. 393;

Lofland v. Cahall (Del.), 118 Atl. 1;

Pratt v. Wilcox (Wash.), 203 Pac. 949;

Paine v. Kentucky Refining Co. (Ky.), 167 S. W. 375;

Santa Clara Min. Ass'n. v. Meredith (Md.), 49 Md. 389, 33 Am. Rep. 264;

Cheeney v. Lafayette B. & M. R. Co. (Ill.), 68 Ill. 570, 18 Am. Rep. 264;

Rogers v. Hastings & Dakota Ry. Co., 22 Minn. 25;

Ten Eyck v. Pontiac, O. & P. A. R. Co. (Mich.), 41 N. W. 905, 3 L. R. A. 378, 16 Am. St. Rep. 633;

Loewer v. Tonoke Rice Mill Co. (Ark.), 161 S. W. 1042;

New Orleans, B. R. & B. S. Packet Co. v. Brown, 36 La. 138, 51 Am. Rep. 5;

Spalding v. Enid Cemetery Ass'n. (Okla.), 184 Pac. 579. [See Appendix p. 23];

Waters v. American Finance Co. (Md.), 62 Atl. 357. [See Appendix p. 25];

Fitzgerald & Mallory Const. Co. v. Fitzgerald, 137 U. S. 100, 34 L. Ed. 608. [See Appendix p. 26];

Gumaer v. Cripple Creek Tunnel, etc. Co. (Colo.), 90 Pac. 81. [See Appendix p. 27.]

This is the rule announced and followed by this Court in

Montana Tonopah Mining Co. v. Dunlap (C. C. A. 9th), 196 Fed. 612. [See Appendix p. 29.]

This Court again followed the same rule in

Denman v. Richardson (C. C. A. 9th), 292 Fed. 19. [See Appendix p. 31.]

The rule is the same in California.

Zellerbach v. Allenberg, 99 Cal. 57, 33 Pac. 786. [See Appendix p. 33];

Bassett v. Fairchild, 132 Cal. 637, 52 L. R. A. 611, 64 Pac. 1082. [See Appendix p. 34];

King v. Grass Valley Gold Mines Co., 205 Cal. 698, 272 Pac. 290.

In the latter case plaintiff corporate officer claimed to have rendered services and to be entitled to compensation therefor as a mining engineer, mine manager and superintendent and was permitted to recover on the theory of *quantum meruit*. [See Appendix p. 39.]

See also:

San Leandro Canning Co. Inc. v. Perillo, 84 Cal. App. 635. [See Appendix p. 39.]

The first case cited by appellant to support its misstatement of the rule is

Finch v. Warrior Cement Corp. (Del.), 141 Atl. 54.

On the point under consideration the only question involved was whether, where a promoter submitting a plan to organize a new corporation to take over the assets of the present corporation, proposed to actively assist in the sale of bonds and in forming a syndicate therefor, the commissions which he received while acting as a director of the corporation for the sale of its bonds were illegally paid and must be returned. The commissions taken by the defendant directors were ten per cent of certain stock sales. The court says:

> "It will not do to say that the ten percent. flotation charge was a reasonable one. The question is, Was it the best that could reasonably have been obtained? It is manifest that, to the extent of the commission paid to Deer and Steward (defendant directors), the brokers were content to take less than the specified ten per cent."

In other words it was specifically found that the defendant directors received more for their services than would have been charged by others and further, "but aside from that, the services rendered in this case do not appear to have required the exertion of any more exceptional or extraordinary efforts than did the services rendered in the Lofland case"

Jones v. Foster (C. C. A. 4th), 70 Fed. (2d) 200,

next cited, has not, so far as we can see, any possible application in its effect to the case at bar. The case was tried in the court below to a jury and the trial judge specifically instructed that the claimed "services performed were clearly not outside the scope of the duties pertaining to the defendant's office as a president of the corporation in accordance with the by-laws." [See Appendix p. 41.]

O'Leary v. Seemann (Colo.), 232 Pac. 667,

was a suit to compel the president and general manager of the corporation to account for the proceeds of a large amount of corporate stock which he had sold. It does not in any way depart from the correct rule as above stated but on its facts is entirely inapplicable to the case at bar. [See Appendix p. 18.]

We submit without comment that

Pindell v. Conlon Corp. (Ill.), 24 N. E. (2d) 882,

has no possible application to the case at bar. [See Appendix p. 41.]

Appellant cites

Larkin v. Enright, 37 N. E. (2d) 905,

an opinion by the Illinois intermediate Appellate Court. This was a suit to restrain defendant from voting two shares of stock, to restrain directors elected by the vote of these two shares from participating in the voting at any meeting of the board, to restrain the collection of certain money owing to the corporation and for other equitable relief. [See Appendix p. 42.]

Similarily under this sub-heading appellant cites

In re Dr. Voorhees Awning Hood Co. (D. C. Pa.), 187 Fed. 611.

This was a proceeding in bankruptcy in connection with which the president of the bankrupt corporation appears to have filed claims against it for salary and other compensation. We can see no possible connection between this case and the one at bar where officers have been paid compensation for services rendered pursuant to due and legal authorization by the board of directors. [See Appendix p. 43.]

It remains perhaps to establish that the devices and inventions developed by Messrs. Miller and Ballagh originated under circumstances which constituted them their individual property both as to the element of use or so-called "shop rights" and also from the proprietary standpoint and that, in conferring their free use upon the corporation and in assigning their present and future proprietary interest thereto, they were parting with property rights of value.

The authorities seem uniform that, prior to the assignment of patents or patent applications or interests, title to the patents or patent rights are in the individual defendants where the contract of employment does not provide otherwise.

> *U. S. v. Dubilier Corp.*, 289 U. S. 178, 77 L. Ed. 1114. [See Appendix p. 43];
>
> *Dysart v. Remington Rand Inc.* (D. C. Conn.), 40 Fed. Supp. 596;
>
> *Geer Grinding Mach. Co. v. Stuber* (Mich.), 276 N. W. 514;
>
> *White Heat Products Co. v. Thomas* (Pa.), 109 Atl. 685;
>
> *Dean v. Hodge* (Minn.), 27 N. W. 917. [See Appendix p. 46];
>
> *Heywood-Wakefield Co. v. Small* (C. C. A. 1st), 87 Fed. (2d) 716. [See Appendix p. 49.]

"(c) *The Inventions of the Defendants cannot be classified as Services.*"

Appellant's argument under this heading is hardly worthy of an answer, and we shall certainly devote but little space to that purpose. Appellant could hardly deny that the royalties paid by defendant corporation to plaintiff from the years 1928 through 1939 totalling $101,-406.61 [Pl. Ex. 18-D] did not have a current value year

by year to plaintiff. If defendant officers had retained their proprietary rights in the patents and devices which they developed for the company beginning about 1939, and the company had been obliged to pay royalties upon them, obviously this would have constituted a charge against the company's revenues. However, the individual defendants devised these inventions with the sole idea and for the sole purpose of improving the company's business and making it the beneficiary in so far as their royalty free use was concerned, and, in addition thereto, conferred the proprietary ownership upon the company. If this does not constitute the rendition of "services" we do not understand the meaning of that term and, in our opinion, this argument of appellant characterizes and should discredit its case *in toto.*

"(d) *Even if the Inventions of the Defendants should be considered, they were not of sufficient Value to support the amount of the Salaries."*

Appellant introduces its argument here by stating that this is an equity case and that the appellate court has the power to review the facts, decide them *de novo,* and overrule the findings of fact made by the trial court. We have already, at too great length no doubt, replied to these contentions.

The record shows the steady and progressive increase in the sales of the inventions and devices year by year from the time they were first manufactured, amounting, generally speaking, to more than a doubling in each successive year. We have detailed the testimony for defendants relative to the value, actual and potential, of these inventions and devices to the corporation. The only testimony *contra* offered by plaintiff was that of the witness Grant [R. 543-548] and its employee, Chestnut [R. 425-427, 565], both called in rebuttal on

this point. A reading of their testimony demonstrates its worthlessness and self-serving character. The trial court had the benefit of seeing and hearing both of these gentlemen as it did the witnesses for the respondents on this issue. On the record as made, we are confident that this Court will not disturb the findings of the trial court on this issue irrespective of whether it has the reviewing power to do so or not, which we maintain it does not have.

"Defendants' Salaries were part of the Conspiracy on the part of Defendants to fraudulently enrich themselves at the Expense of Plaintiff, the minority Stockholders."

Here again, just as in its complaint, appellant makes an *assertion* of "fraudulent conspiracy." The mere bald assertion, however, is all that it offers on the point. The record is devoid of any evidence to support it.

There were many reasons, from the standpoint of a wise and conservative business policy, why defendant corporation stopped paying dividends when it did. These reasons appear in the record as evidence produced by defendants as against a total lack of any evidence on the point produced by plaintiff. The court will undoubtedly take notice of the fact that at the beginning of 1939 all business was faced with uncertainty. Those operating to any extent in the export trade and, even more, those manufacturing items made of rubber, as was this company, might be considered to have been facing more than an uncertainty. Certain fortunate subsequent developments as to the rubber situation were purely fortuitous and could not have been foreseen at that time. The matter of dividends was discussed at a directors' meeting on November 29, 1940 at which time Dulin offered his opinion that the company was in a position to declare and pay a dividend. Naturally, as president of the plain-

tiff, he desired it to participate further in the "gravy" it had been enjoying from defendant company for years. Directors Ballagh and Miller, however, were of the opinion that no dividend should be declared at that time in view of the company's requirements for accumulating a rubber reserve, intended plant expansion, "the requirement of paying royalties on protectors manufactured and sold and the validity of the patents on its manual and hydraulic applicators" [R. 255, 256]. Defendant Ballagh gives as one of Mr. Miller's reasons for suspending dividends the necessity of creating a reserve against the litigation instituted by plaintiff for royalty on the Bettis-Hopkins patent licensing agreement and, as his own reasons, the critical war situation, contemplated expansion, attempts to get into war work, and inadequate cash on hand [R. 361]. Mr. Miller states that he was responsible for suspending dividends [R. 382] and his reasons therefor were contemplated plant expansion (two lots had actually been purchased), the war situation, the necessity of conserving capital, the fact that the company operated on a cash basis without the use of credit, and the Byron-Jackson royalty suit [R. 383].

All of these reasons were substantial and valid. They appealed to four out of five directors as being so and the Board acted upon them as a Board. The only dissenting director was plaintiff's president, Dulin, who obviously had a palpably direct personal interest in conflict with the best interests of the corporation of which he was, in name, a director.

The decision by the Board of Directors as to dividends was one of corporate policy purely within its jurisdiction and, in the absence of fraud, of which there is no scintilla of evidence in the case, neither this nor any other court can interfere with this determination of policy by the directors. The authorities which we have heretofore cited and quoted from, are uniform on this subject.

Ratification and Waiver.

In paragraph 21 at page 12 of its brief an assertion is made that Miller was overpaid in 1940 in the sum of $7750.00. The facts are that in 1940 (Dec. 1, 1939 to Dec. 1, 1940) he received a total compensation of $19,252.00. At the directors' meeting of March 18, 1940 he was voted an annual salary of $1,500 per month commencing March 1, 1940, Director Dulin being present and voting therefor. Whatever may be the law elsewhere, in California transactions between a corporation and its directors are neither void nor voidable if the fact of a beneficial interest to the director involved therein is disclosed to or known by the shareholders and they ratify the transaction in good faith by a majority of those entitled to vote. (Civil Code, Sec. 311 (b).)

Thus, in the absence of actual fraud, the various ratifications at the stockholders' meetings in the case at bar are controlling. See:

> *Russell v. Patterson* (Pa.), 81 Atl. 136;
>
> *Middletown v. Arastraville Min. Co.,* 146 Cal. 219.

In the latter case the court announced the general rule that *stockholders occupy no such fiduciary relationship to each other as to preclude a stockholder from voting at a stockholders' meeting upon any question in which he has an individual interest adverse to the other stockholders.* [See Appendix p. 52.]

All actions of the Board of Directors for the years 1939 and 1940 were ratified at the subsequent annual meetings of the stockholders by a vote of three-quarters of the outstanding stock [R. 232, 234, 261-265], excepting that, for the year 1941, the record does not show the proceedings of the annual stockholders' meeting at the conclusion of that year since this suit was instituted before its termination.

At the annual stockholders' meeting on January 21, 1941 [R. 261] Dulin, with full knowledge previously acquired at directors' meetings of his fellow-directors' ideas as to the worth of the services of Messrs. Miller and Ballagh, seconded a motion electing the same directors for the ensuing year and voted in favor of it. At the directors' meeting of the same date [R. 267], Dulin voted for the re-election of the same officers, which vote, by every fair implication, carried with it an approval of their compensation at the current rate and a waiver of any objections thereto. Dulin was absent at both the stockholders' and directors' meetings held on January 16, 1940 at the end of the fiscal year 1939 though he had received due notice thereof [R. 232-238]. Dulin knew the attitude of the directors on the compensation question and if he did not agree with them, it was his duty to propose other directors and officers at both the stockholders' and directors' meetings which he attended. Similar action has been condemned and held to be a ratification and waiver in

> *Klein v. Independent Brewing Assn.* (Ill.), 83 N. E. 434. [See Appendix p. 52], and
>
> *Nahikian v. Mattingly* (Mich.), 251 N. W. 421.

Under these circumstances we submit that plaintiff is in no position to complain as it does here.*

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*In a footnote at page 6 of its brief appellant states that defendant Miller received $19,252 for 1940 and $13,500 for 1941 up to September 10. Nothing is said as to 1939 nor could it well be since Miller's compensation in that year was authorized and voted for by director Dulin, plaintiff's representative [R. 213]. At the directors' meeting of March 18, 1940 [R. 240] Dulin approved and voted for an increase for Miller from $1,000 to $1,500 per month commencing March 1st. From December 1, 1939, the beginning of the fiscal year, to March 1, 1940 Miller received $3,000, or $1,000 per month which compensation Dulin had previously voted for and approved [R. 214]. From March 1, 1940 to December 1, 1940 Dulin had voted for and approved Miller's compensation in the sum of $13,500, or at the rate of $1,500 per month, or a total of $16,500 for the twelve months. Miller actually received $19,252 for the twelve months because he was voted a bonus equal to two months' pay at a directors' meeting at which Dulin was absent [R. 252]. For the period from December 1, 1940, to September 10, 1941, Miller received $14,000, being the exact amount authorized by the board for that period with the approval and affirmative vote of Dulin. Consequently for the whole period from December 1, 1939, to September 1, 1941, the amount received by him in excess of Dulin's own authorization and vote is only $2,752 and not $7,750 as claimed by appellant and stated in the footnote, text and complaint.

Conclusion.

It is unfortunate that the record in this case cannot and does not portray the subsequently demonstrated wisdom of the policy adopted by defendant company's directors in investing money, time and effort, the latter being supplied by the individual defendants Miller and Ballagh, inventing and devising new articles of manufacture and sale and in placing them on the market to supplant the serious loss in business necessarily resulting from the invalidation of the Bettis patent. If the court were at all in doubt as to the wisdom and good faith of the directors in adopting the policy which they honestly did for the welfare of the corporation, it might well remand the case to the District Court for the purpose of supplementing the record by bringing the company's history up to date.

Notwithstanding that this is purely an action at law, the equities are all with the respondents. Appellant purchased one-quarter of the total capital stock of the respondent company in September, 1928, paying therefor a total of $25,000 [R. 61]. Since that time and up to the end of 1939 it has realized a total of $221,906.61 in cash on that investment or almost one hundred per cent a year [Pl. Ex. 18-D]. Plaintiff has rendered no services whatever nor anything useful of any kind to defendant company since the failure of the Bettis patent in 1932. It still, however, desires large dividends and also royalty payments on the invalidated patent, and its "representative" Dulin sits on the company's Board of Directors, apparently for the sole purpose of obtaining dividends and royalty payments for the benefit of the plaintiff of which he is president. If this were, indeed, a suit in equity, we suggest that plaintiff's position and the conduct of its "representative" on defendant corporation's Board is hardly one which would commend itself to a court of

equity. It complains because of compensation paid to company employees and officers who are rendering invaluable service to the company and, in fact, enabling it to survive, the admitted reason for the complaint being a temporary cessation of dividends to itself on an investment for which it has been repaid nearly ten times over.

The trial Court made findings of fact and conclusions of law in no uncertain terms. It found specifically that the individual defendants did not in any way dominate the Board of Directors [R. 62]; that both individual defendants have "at all times * * * discharged their duties as such officers faithfully, efficiently, conscientiously, loyally and meritoriously" [R. 63]; that the services rendered by Messrs. Ballagh and Miller "are now and will continue to be a very great value to said corporation"; that as to each of them the compensation for the period involved "was fair, just and reasonable as to defendant Patterson-Ballagh Corporation at the various times it was authorized, approved and paid," [R. 64-67], and in no case did either Mr. Miller or Mr. Ballagh vote upon a resolution affecting his own compensation [R. 64-67].

On this record it is clear:

(1) That there is no proof of fraud, conspiracy or other tortious act, and that the evidence compels a finding otherwise.

(2) That there is no proof that the compensation paid the individual defendants was either unfair or unreasonable. The evidence compels the conclusion that it was fair and reasonable and that the corporation obtained value received therefor.

(3) That, in the absence of fraud, the Court has no visitorial powers to interfere with determinations of

policy by a corporate board within the sphere of its jurisdiction.

(4) That plaintiff has no standing to complain in equity if this be regarded as a suit in equity.

(5) That if it be regarded as an action at law, plaintiff has wholly failed to prove its case as alleged in its complaint by a preponderance of the evidence or otherwise.

For all the reasons foregoing, we respectfully submit that the Findings, Conclusions and Judgment of the trial court should be affirmed.

Respectfully submitted,

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APPENDIX.

For the convenience of the Court and in conformity with Rule 20(f) we quote hereafter pertinent excerpts from cases cited in the brief, under appropriate headings.

Scope of the Reviewing Powers of the Circuit Court of Appeals on This Appeal.

Excerpts From Cases Cited on Page 9 as to Limitations Upon the Appellate Court.

Cherry-Burrell Co. v. Thatcher (C. C. A. Mont., 9th Cir., 1940), 107 F. (2d) 65 (Br. p. 9):

> "This is simply a case of a conflict in the evidence, and the court below reached its conclusion by determining the weight of the evidence and the credibility of witnesses. Giving due regard 'to the opportunity of the trial court to judge of the credibility of the witnesses' as we are required to do, Federal Rules of Civil Procedure, Rule 52(a), 28 U. S. C. A. following section 723c, we cannot say that the findings are 'clearly erroneous.' We cannot, therefore, set aside the findings."

Storley v. Armour & Co. (C. C. A. 8th, 1940). 107 F. (2d) 499 (Br. p. 9):

> "It is unnecessary to set out the evidence in detail, since it is elementary that a finding by a trier of the facts based upon conflicting evidence will not be disturbed by an appellate court. H. H. Cross Co. v. Simmons, 8 Cir., 96 F. 2d 482, 486; Crowell v. Baker Oil Tools, 9 Cir., 99 F. 2d 574, 577."

Crowell v. Baker Oil Tools Inc. (C. C. A. 9th), 99 F. (2d) 574 (Br. p. 9):

> "Appellant contends that he granted the license to appellee by mistake, because he gave his consent, or granted the license, on the understanding that appellee was granting him a license to use ball valves; that therefore he had rescinded the license granted appellee pursuant to the above quoted statute, and the court below could not bring it into being again. This contention is based on the premise that appellant gave his consent by mistake. The trial court found to the contrary. Although appellant's testimony supports his contention. Mellin's testimony is contrary. *In view of the conflict, we believe the trial court made no 'serious or important mistake' and that its finding was not 'clearly erroneous.'* Furrer v. Ferris, 145 U. S. 132, 134, 12 S. Ct. 821, 36 L. Ed. 649; National Reserve Ins. Co. v. Scudder, 9 Cir., 71 F. (2d) 884; Collins v. Finley, 9 Cir., 65 F. 2d 625, 626; United States v. McGowan, 9 Cir., 62 F. 2d 955, 957, affirmed 290 U. S. 592, 54 S. Ct. 95, 78 L. Ed. 522; Clements v. Coppin, 9 Cir., 61 F. 2d 552, 558; Exchange National Bank v. Meikle, 9 Cir., 61 F. 2d 176, 179; Jones v. Jones, 9 Cir., 35 F. 2d 943, 945; Easton v. Brant, 9 Cir., 19 F. 2d 857, 859; Gila Water Co. v. International Finance Corporation, 9 Cir., 13 F. 2d 1, 2; Rules of Civil Procedure, rule 52(a), 28 U. S. C. A. following section 723c.
>
> "It is also contended that the license granted appellee by appellant was rescinded on the further ground that appellant's consent was obtained by Mellin's fraud. *We think the trial court's finding to the contrary must be sustained, because the evidence, at most, was conflicting only.*" (Italics ours.)

State Farm Mut. Automobile Ins. Co. v. Bonacci, 111 Fed. (2d) 412 (Br. p. 9):

> "The facts largely relied upon in this case consist of testimony and written statements given or made by the defendants not in the presence of the lower court but in the course of the trial of the damage actions in the state court. The lower court, as to such evidence, had no better opportunity of judging the credibility of the witnesses than does the appellate court."

The opinion of Judge O'Brien proceeds (Br. p. 15):

> "The same principle has been accepted in this State in Holmes v. Camp, 180 App. Div. 409, 412, 167 N. Y. S. 840. In an action for damage to property the six-year statute applies *even in those instances where the alleged remedy may be equitable in form.* Keys v. Leopold, 241 N. Y. 189, 192, 149 N. E. 828." (Italics ours.)

Excerpts From Cases Cited on Whether the Action Is One at Law or in Equity. (Br. pp. 15-18.)

Cwerdinski v. Bent, 11 N. Y. Supp. (2d) 208 (Br. p. 15):

> "The purpose of the first cause of action is to compel the parties who were the recipients of the bonus to return to the corporation the difference between the sums actually received by them and the amounts which should have been paid under the bonus plan. In short, the first cause of action involves sums of money which these appellants, and other individual defendants, are said to have received wrongfully from the New Jersey Corporation. Since that is so, the corporation could have instituted an

action for money had and received, and consequently no accounting would have been necessary. Had the corporation brought the action the six-year statute of limitations would have controlled. A shareholder is in no better position than the corporation, even though the complaint is addressed to the equity side of the court."

Wallace v. Lincoln Savings Bank (Tenn.), 15 S. W. 448, 24 Am. St. Rep. 625 (Br. p. 16):

" 'This kind of suit is, at last, but the suit of the corporation for its benefit and upon its right of action. If for any reason the corporation is estopped from suing, or its action is barred, the suit by the stockholder or creditor is likewise affected,' "

In the course of his opinion Judge Lurton quotes with approval an excerpt from Morawetz on Corporations, as follows:

" 'A suit of this character is brought to enforce the corporate or collective rights, and not the individual rights of the shareholders. It may therefore properly be regarded as a suit brought on behalf of the corporation, and the shareholder can enforce only such claims as the corporation itself could enforce. Moreover, the essential character of a cause of action belonging to a corporation remains the same, whether the suit to enforce it be brought by the corporation or by a share-holder. Thus a legal right of action would not be treated as an equitable one, or become governed by the rules applicable to equitable causes of action, as to limitations, etc., because a shareholder has brought suit in equity to enforce it on behalf of the company.' "

Becker v. Empire Power Co., 31 N. Y. S. (2d) 914 (Br. p. 16):

"In other words, if the unconscionable and unlawful gains obtained by miscreant directors and officers are known to be in a fixed amount and do not exceed the correlated loss suffered by the corporation, then there is no occasion or necessity for resort to an equitable action for an accounting: the amount being known, an action at law for money had and received will lie and is the proper remedy. I so interpret Dunlop Sons, Inc. v. Spurr, 285 N. Y. 333, 336, 34 N. E. (2d) 344. In the case at bar the extent of the illegal gains of Phillips and Olmsted and consequent loss to the corporation was definitely known for paragraph VI of the complaint expressly alleges that they directed into their own pockets the sum of $7,385,075; that being a known fact, and the gains obtained by Phillips and Olmsted and the consequent loss to the corporation being the same in amount, there was no need, therefore, to sue for an accounting and there existed a full, adequate and complete remedy at law to sue for money had and received and the six-year statute would apply."

Dunlop v. Dunlop, 34 N. E. (2d) 344 (Br. p. 16):

"Potter v. Walker, 276 N. Y. 15, 11 N. E. 2d 335, did not decide that the ten-year Statute of Limitations (Civil Practice Act, §53) is necessarily applicable to all cases in which corporate directors have profited in any degree through a breach of their fiduciary duties. In such a case an action for an accounting may be brought only for the recovery of gains received by the directors beyond the amount of losses caused to the corporation by their wrong. Where, as in the present case, the gains received

by the directors do not exceed the correlated losses suffered by the corporation, no accounting is necessary and the Statute of Limitations, Civil Practice Act, §48, which controls the remedy at law is to be applied. See Goldstein v. Tri-Continental Corporation, 282 N. Y. 21, 24 N. E. 2d 728."

Gormley v. Slicer (Ga. Sup. Ct.), 172 S. E. 23 (Br. p. 17):

Paragraphs 1 and 2 of the Supreme Court's opinion on certification read:

"1. The facts show essentially an action at law for damages based on tort, without any grounds for equitable relief." (Citing many cases.)

"2. The fact that it was alleged in the petition and in the motion to refer the case to the auditor and in the motion to recommit the case to the auditor, that the case was one in equity, and that the judge in deciding the case considered it was in equity and it was so recited in the bill of exceptions, considered in connection with other facts set forth in the second question propounded by the Court of Appeals, did not make the case one in equity. The second question propounded by the Court of Appeals is answered in the negative."

Potter v. Walker, 287 N. Y. S. 812 (Br. p. 17):

"The following principles appear to be established:

"First, that, as the right of the stockholder is derivative, the period of time within which he may sue is measured by the rule which would be applied if his corporation had brought the suit. Brinckerhoff v. Bostwick, *supra;* Pollitz v. Wabash R. Co.,

207 N. Y. 113, 100 N. E. 721; Curtis v. Connly, 257 U. S. 260, 42 S. Ct. 100, 66 L. Ed. 222.

"Second, that the directors of a corporation being held to the liability of trustees as to the care of corporate property may be sued in equity for an accounting for any dereliction of duty. Bosworth v. Allen, 168 N. Y. 157, 61 N. E. 163, 55 L. R. A. 751, 85 Am. St. Rep. 667; Asphalt Construction Co. v. Bouker, 150 App. Div. 691, 135 N. Y. S. 714, affirmed 210 N. Y. 643, 105 N. E. 1080. However, they are trustees of an implied or constructive, rather than an express, trust and therefore the jurisdiction of equity is concurrent and not exclusive. Pomeroy Eq. Juris (4th Ed.) §157.

"Third, that even where a suit in equity *for an accounting* is permissible if a legal as well as an equitable remedy exists as to the subject-matter of the suit, *the limitation, applicable to the legal remedy must be applied.* Kane v. Bloodgood, 7 Johns. Ch. 90, 11 Am. Dec. 417; Keys v. Leopold, *supra;* Dumbadze v. Lignante, *supra.*

"Fourth, that a corporation as distinguished from its stockholders may sue its directors at law *where only legal relief is sought.* O'Brien v. Fitzgerald, 143 N. Y. 377, 38 N. E. 371; Dykman v. Keeney, 154 N. Y. 483, 48 N. E. 894.

"In the light of these principles, considering the causes of action attacked, does it appear that as to the subject-matter of any of them the plaintiff had a legal as well as an equitable remedy?" (Italics ours.)

Emerson v. Gaither (Md.), 64 Atl. 26 (Br. p. 18):

"First. The authorities are not uniform as to how far a court of equity has jurisdiction in suits by corporations, or their receivers, against directors who were guilty of negligence or of acts contrary to some statutory provision. It cannot be denied that there may be charges of mismanagement or negligence, causing loss or injury to the corporation, for which there could be no reason for going into equity; the corporation having a complete and adequate remedy at law. In 3 Clark & Marshall on Cor., §755, it is said that 'the corporation may maintain an action at law against them at common law—an action on the case—to recover damages'; but those authors go on to say: 'Or it may maintain a suit in equity *when any special ground of equitable jurisdiction exists, as in a case where an accounting or discovery or injunction is necessary.*' Judge Thompson, in the article written by him on Corporations in 10 Cyc., thus speaks of the subject, on page 836: 'The proper remedy is said to be an action at law for damages, and not a bill in equity, where no accounting of the financial condition of the corporation is necessary to determine the extent of their liability. The jurisdiction of courts of equity to compel unfaithful directors to account to the corporation, or to its representative, for frauds and breaches of trust has been well established since the time of Lord Hardwicke, and unquestionably this is a proper forum in nearly all such cases, although this statement does not exclude the jurisdiction of courts of law in cases appropriate for the exercise of that jurisdiction; the two remedies being often concurrent.'" (Italics ours.)

Corsicana Nat. Bank v. Johnson (C. C. A. 5th), 218 Fed. 822 (Br. p. 18):

"The bill in this case charged the defendant, who had been an officer of the plaintiff bank, with liability for the loss sustained by the bank on a loan of its funds in an amount which exceeded one-tenth of the amount of the bank's paid-in capital and surplus, the ground of the asserted liability of the defendant being his alleged participation in and responsibility for the violation of the statutory prohibition of such a loan. 5 Fed. Stat. Ann. 139, 34 Stat. 451. The suit was the assertion of the right of the bank to hold the defendant liable in his personal and individual capacity for all damages sustained by the bank in consequence of the defendant knowingly violating the provision of the above-mentioned statute. Rev. Stat. U. S. §5239. Plainly a suit to recover damages so sustained may be maintained at law, *and is not cognizable by a court of equity, in the absence of any showing of the inadequacy of the legal remedy which is available.* Cockrill v. Cooper, 86 Fed. 7, 29 C. C. A. 529; Stephens v. Overstolz (C. C.), 43 Fed. 465.

"In the case at bar no fact was alleged or proved which tended to show any inadequacy of the legal remedy to which the plaintiff might have resorted. The plaintiff's claim was that it had lost the total amount loaned, less what had been and what might yet be realized from certain corporate stock which it had received in a settlement of the bankrupt estate of one of the insolvent borrowers. The holding of that stock by the plaintiff constituted no ground for a resort to a court of equity. The bank's claim was subject to be reduced by the amount already realized on that stock and by the reasonable value of it, if it still represents anything of value. This abatement

of the amount of damages recoverable could be made in a court of law as well as in a court of equity. It was simply a matter of showing the actual loss sustained by the plaintiff as a result of the forbidden loan. It was not made to appear that in a court of law there was any obstacle in the way of proving and recovering the damages sustained. In short, we discover no equitable feature in the claim sought to be enforced. *It was a simple legal demand for damages, to be assessed in a judgment for money.* The suit in equity could not properly be maintained because the case was one where a plain, adequate, and complete remedy may be had at law for the wrong complained of. Southern Pacific R. R. Co. v. United States, 200 U. S. 341, 26 Sup. Ct. 296, 50 L. Ed. 507; Smyth v. N. O. Canal & Banking Co., 141 U. S. 656, 12 Sup. Ct. 113, 35 L. Ed. 891." (Italics ours.)

Excerpts From Cases Cited Establishing That in Any Event the Burden of Proof Is Upon Plaintiff.

Nahikian v. Mattingly (Mich.), 251 N. W. 421 (Br. p. 26):

"The fixing of the salary of defendant by the board of directors may have been ill-advised action. considering the financial condition of the corporation and the character of the services of the president, but it was a matter of corporate management, vested in the directors, and their action, *in the absence of fraud or willful or wanton departure from known or manifest duty, bars judicial substitution of opinion.*

"In McKey v. Swenson, 232 Mich. 505, 205 N. W. 583, we held action in fixing salaries wholly void and cast the burden upon the officers to give the court in-

formation upon which reasonable compensation could be fixed. Such, however, is not the case at bar, for here we do not have wholly void action *but only assertion of unreasonable compensation* and the burden is on plaintiff to establish the charge.

"As said in Burden v. Burden, 159 N. Y. 287, 54 N. E. 17, 23: 'The plaintiff is in the position of all minority stockholders, who cannot interfere with the management of the corporation so long as the trustees are acting honestly and within their discretionary powers.'

"A minority complaining stockholder, if he avers excessive salary, *must show facts establishing unjustifiable oppression in such respect.* The evidence fails to show that salary voted defendant, by the board of directors was so unreasonable or excessive, under the circumstances, as in itself to be deemed fraudulent and, therefore, authorizing restoration in whole or in part. We may not readjust the salary without a yardstick applicable to the particular circumstances and not even then upon mere difference of opinion from that of the board of directors, *but only upon concrete proof that the salary evidences wrongdoing or inexcusable oppression to the point of being fraudulent.* Less than this would constitute an intolerable interference with legitimate internal corporate management.

"It is a well-settled rule of law that the authority of the directors is absolute when they act within the law, and that questions of policy and internal management are, in the absence of nonfeasance, misfeasance, or malfeasance, left wholly to their decision. *Ratification by the board of directors of an increase in defendant's salary, if made in good faith and be-*

lieved to be for the best interest of the company, validated the increase. Decree as to salary reversed." (Italics ours.)

Chapman v. Troy Laundry Co. (Utah), 47 Pac. (2d) 1054 (Br. p. 26):

"If we assume that there was bad faith in the minds of the directors on the 8th, then it would seem to follow that they must have, for some reason, relied on Kilpatrick. But to assume the fact is to eliminate the necessity for proof. Our assumptions must be to the contrary until proof overcomes them."

Bodell v. General Gas & Elec. Corp. (Del.), 132 Atl. 442 (Br. p. 27):

"I do not understand the defendants to argue that the action of the directors in this particular is not reviewable. They do insist, however, that inasmuch as the matter of the issuance of the stock was placed by the certificate of incorporation in their control, the general principle which excludes stockholders from matters of management *and accords to the acts of the directors a presumption in favor of their propriety and fairness, is to be here applied. This is true."* (Italics ours.)

Cole v. National Cash Credit Ass'n (Del.), 156 Atl. 183 (Br. p. 27):

"There is a presumption that the judgment of the governing body of a corporation, whether at the time it consists of directors or majority stockholders, is formed in good faith and inspired by a *bona fides* of purpose. Robinson v. Pittsburgh Oil Refining Corp., 14 Del. Ch. 193, 126 A. 46; Davis v. Louisville Gas & Electric Co., 16 Del. Ch. 157, 142 A. 654."

Karasik v. Pacific Eastern Corp. (Del.), 180 Atl. 604 (Br. p. 27):

> "There is a presumption, rebuttable of course, that the directors of a corporation are actuated in their conduct of the business of the corporation by a *bona fide* regard for the interests of the corporation. Mercantile Trading Corp. v. Rosenbaum Grain Corp., 17 Del. Ch. 325, 154 A. 457; Davis v. Louisville Gas & Electric Co., 16 Del. Ch. 157, 142 A. 654; Finch v. Warrier Cement Corp., 16 Del. Ch. 44, 141 A. 54; Robinson v. Pittsburgh Oil Refining Corp., 14 Del. Ch. 193, 126 A. 46. An honest mistake of business judgment on the part of directors is not reviewable by courts. This is the general rule and it is supported by the decision of the Supreme Court of this State in Bodell v. General Gas & Electric Corp., 15 Del. Ch. 420, 140 A. 264."

Anderson v. Bean (Mass.), 172 N. E. 647, 72 A. L. R. 959 (Br. p. 27):

> "The general principle is that stockholders have no individual interest in the profits of a corporation until a dividend has been declared, that the accumulation of a surplus does not of itself entitle stockholders to a dividend, that the time when a dividend shall be declared and its amount rest in the sound discretion of the corporation or its authorized officers, usually the board of directors, that the action of such officers will not be disturbed if taken in good faith according to law and not in plain violation of the rights of stockholders, and that rational presumptions will be indulged in favor of the honest, decision of such officers. Tax Commissioner v. Putnam, 227 Mass. 522, 537, 116 N. E. 904, L. R. A. 1917F, 806; Fernald v. Frank Ridlon Co., 246 Mass. 64, 71, 140 N.

E. 421; Nutter v. Andrews, 246 Mass. 224, 227, 142 N. E. 67; Lee v. Fisk, 222 Mass. 418, 421, 109 N. E. 833; Thomas v. Laconia Car Co., 251 Mass. 529, 535, 146 N. E. 775; Boston Safe Deposit & Trust Co. v. Commissioner of Corporations and Taxation, 262 Mass. 1, 5, 159 N. E. 536; Adams v. Eastern Massachusetts Street Railway, 257 Mass. 115, 131, 153 N. E. 466; Morse v. Boston & Maine Railroad, 263 Mass. 308, 311, 160 N. E. 894 67 A. L. R. 758. It is urged that the case at bar constitutes an exception to the general rule *because the trustee owning one-half the stock in his own right and one-half as trustee was in absolute control of the corporation* and was bound to do what a court of equity may think he ought to have done in way of declaration of dividends, and that to this end the corporate entity ought to be regarded as a fiction. This contention cannot be supported. The trustee acted in good faith." (Italics ours.)

Winberg v. Camp Taylor Dev. Co. (Ky.), 95 S. W. (2d) 261 (Br. p. 28):

"It does not devolve upon the officer or director whose compensation is in question to prove that the compensation is fair, but the objecting stockholder *must establish affirmatively* that the compensation is unreasonable, and these facts must be shown by the pleadings as well as the proof. Beha, *et al.* v. Martin, *et al.,* 161 Ky. 838, 171 S. W. 393." (Italics ours.)

Borg v. International Silver Co., 11 Fed. (2d) 147 (Br. p. 29):

"The Colt transaction may have been improper; we cannot try it here. The first proposed sale, which

was enjoined, we may assume to have been improper. Together we will not say that they throw no suspicion on the directors' motives. But suspicion is hardly enough, unless the balance of advantage weighs very strongly in the plaintiffs' favor."

Noel v. Parrott (C. C. A. 4th), 15 Fed. (2d) 669, cert. den. 47 S. Ct. 457, 273 U. S. 754, 71 L. Ed. 875 (Br. p. 29):

"It needs neither argument nor citation of authority to establish the proposition that the directors were without authority to give away the corporate assets, and that for them to make to several of their members and other persons a gift of a large sum of money from the corporate assets would be neither 'wise' nor 'proper,' and would amount to an illegal misapplication of corporate funds. *We must assume that the directors did not intend such a flagrant violation of their trust.* Delaware, L. & W. R. Co. v. Kutter (C. C. A. 2nd), 147 F. 51, 77 C. C. A. 315; Hobbs v. McLean, 117 U. S. 567, 6 S. Ct. 870, 29 L. Ed. 940; U. S. v. Cent. Pac. R. Co., 118 U. S. 235, 6 S. Ct. 1038, 30 L. Ed. 173." (Italics ours.)

Gray Corp. v. Meehan (C. C. A. 1st), 54 Fed. (2d) 223 (Br. p. 29):

"When acts are done by officers of a corporation apparently authorized to perform them, in the absence of a public statute or charter to the contrary, the presumption is in favor of their regularity. The burden is on those who claim the contrary to prove affirmatively otherwise."

Fornaseri v. Cosmosart Realty Etc. Corp., 96 Cal. App. 549 (Br. p. 30):

> "Every presumption is in favor of the good faith of the directors. Interference with such discretion is not warranted in doubtful cases. In *Gamble v Queens County Water Co.,* 123 N. Y. 91 (9 L. R. A. 527, 25 N. E. 201), it is said: 'To warrant interference by a court in favor of minority stockholders . . . a case must be made out which plainly shows that such action is so far opposed to the true interests of the corporation itself as to lead to the clear inference that no one thus acting could have been influenced by any honest desire to secure such interest, but that he must have acted with an intent to subserve some outside purpose, regardless of the consequences to the company.' "

Michaels v. Pacific Soft Water Laundry, et al., 104 Cal. App. 366 (Br. p. 31):

> "The general rule is that the testimony of a witness cannot be wholly disregarded, but that unless it is impeached or contradicted by other testimony, by some presumption, or by an inference deducible from the facts proved, or unless it is inherently improbable, the trial court must accept it as true. (10 Cal. Jur. 1143; *Stewart v. Silva,* 192 Cal. 405, 410 (221 Pac. 191), concurring opinion; *Sun-Maid Raisin Growers v. Papazian,* 74 Cal. App. 231, 239 (240 Pac. 47).) *This rule is particularly applicable to a case such as we have here where the issue is fraud or good faith.* The presumption against fraud, which approximates the presumption against crime (*Truett v. Onderdonk,* 120 Cal. 581, 588 (53 Pac. 26)), the presumption that private transactions have been fair and regular. and the presumption that the ordinary course of

business has been followed (sec. 1963, subds. 1, 19 and 20, Code Civ. Proc.) are all *evidence* of good faith of the bank in this particular, and a contrary finding cannot stand without some evidence rebutting them." (First italics ours.)

Clark v. Oceano Beach Resort Co., 106 Cal. App. 574 (Br. p. 31):

> "At most the evidence raises a suspicion that one of the motives of the defendant Long was to gain control of the corporation."

On the question of presumptions and burden of proof, the court says:

> "Whether an assessment shall be levied or the property of a corporation shall be sold to raise funds with which to meet its obligations is a question for the determination of the corporation and its officers and not for the courts. 'It will be presumed that assessment were made in good faith and for a proper purpose. And if the purpose is a proper one the motive of the directors in levying it is immaterial.' (Fletcher's Cyclopedia of Corporations, sec. 4273.)"

Excerpts From Cases Cited by Appellant on the Issue of Burden of Proof.

Booth v. Beattie (N. J.), 118 Atl. 257 (Br. p. 35):

> "The two managing directors have not been overpaid. In my judgment their services to the company since the adoption of the resolution were worth at least what they received. The company could, no doubt, hire managers at less pay, much less, but not managers who could produce results as these did. *They could be replaced, but not duplicated.* They are not merely carpet men, but Beattie carpet men, skilled

and trained to make and market Beattie rugs—a distinctive line in the trade and at the top." (Italics ours.)

Sotter v. Coatesville Boiler Works, et al. (Pa.) 101 Atl. 744 (Br. p. 35):

"If courts may depart at will from the rule just stated, and substitute their judgments for the legally exercised discretion of the directors of private business corporations, in determining the question of future compensation to be paid to the latter's employees, then there is no reasonable limit to the right of judicial interference with corporate management; but, fortunately, this is not the law."

Church v. Harnit, 35 Fed. (2d) 499 (Br. p. 40):

"As to the allowances made to Harnit by a board of directors, of whom three may be said to have been collaterally interested adversely to the corporation in that they themselves were to receive an allowance of bonus from Harnit, this does not wholly invalidate the action of the board. As directors, these three occupied a fiduciary relation toward the minority stockholders. Their action was open to the most careful scrutiny by the court. The burden is on them and upon Harnit to show that the contract was fair, honest, and reasonable in all respects, and especially with reference to the rights of the minority."

O'Leary v. Seemann (Colo.), 232 Pac. 667 (Br. pp. 42, 71):

"Counsel for Seemann claimed that services outside the regular duties of an officer give rise to a right of action for *quantum meruit.* We think that is so when there is a request to him to do the work or its equivalent (Mining & Milling Co. v. Prentice,

25 Colo. 4, 52 P. 210; Brown v. Silver Mines, 17 Colo. 421, 30 P. 66, 16 L. R. A. 426; Cheeney v. Lafayette, etc., R. W. Co., 68 Ill. 570, 575, 18 Am. Rep. 584; Corinne, etc., Co. v. Toponce, 152 U. S. 405, 14 S. Ct. 632, 38 L. Ed. 493); otherwise not. If it could be done without a request, any officer could involve a company to any extent of his own free will. *Since the resolution is not shown to have been passed, there is no request, and there is no subsequent vote,* as in Gumaer v. Cripple Creek, etc. Mining Co., 40 Colo. 1, 90 P. 81, 122 Am. St. Rep. 1024, 13 Ann. Cas. 781. But aside from that there is no showing of the value of the services of the defendant Seemann in selling the stock. This is for him to show. If the showing had been made, it is possible that the retention of the fruits of his services would have amounted to an implied contract as in Waters v. American Finance Co., 102 Md. 212, 62 A. 357." (Italics ours.)

Raynolds v. Diamond Mills Paper Co. (N. J.), 60 Atl. (Br. p. 58):

"But my conclusion is that no case is presented under the general equity power of the court, in which an equity judge should intervene and direct the distribution of profits in the form of dividends to these stockholders, setting aside the action for determination of the board of directors."

The court further said:

"As I recall it the fifth director, Mr. Raynolds, never qualified and the fourth director is a mere dummy, holding one share of stock in order to qualify. Messrs. Thompson, Van Gilder and Ralph Thompson, therefore, as a board of directors or con-

trolling the board of directors, *have fixed their salaries themselves at the sums that I have mentioned.*" (Italics ours.)

Article 3, Section 1, of the by-laws of Patterson-Ballagh Corporation, the heading whereof is "Officers and their duties" reads in part (Br. p. 59):

> "The officers of this corporation shall be chosen by the directors and shall consist of a president, vice-president, secretary, treasurer, and such other officers as may be required by law or may be created by the board of directors."

Lillard v. Oil Paint & Drug Co. (N. J.), 56 Atl. 254 (Br. p. 63):

> "Defendant's claim that the salary of $18,000 is reasonable and fair, although the same services had been previously rendered to the company for about half that sum, is based mainly on the contention that the defendant, at the time of assuming the management, was making as much or more in other business, and the conclusiveness of the previous smaller salary paid is answered, or attempted to be answered, by the contention that the profits received by Lillard, through the receipts of which he paid for his stock, should be taken as really salary paid to him. Neither of these contentions is sound."

Excerpt From Argument Presented in the Trial Court. (Br. p. 65.)

> "When Mr. Dulin stated in his letter of March 27, 1940, that, on the basis of $232,000 of sales, $36,000 of combined executive salaries were all the business could stand, he did not include in said salaries any compensation for any inventions assigned to or used by the corporation royalty free.

"In 1940 Mr. Miller received a total compensation of $19,750. Mr. Dulin voted for the resolution awarding $18,000 of this compensation. In addition in his letter of March 27, 1940, Mr. Dulin states in substance that on the basis of $232,000 of sales $18,000 per year for Mr. Miller is not too much. Actually in 1940 the gross sales amounted to approximately $329,600, and the net sales to approximately $300,800. In 1941 Mr. Miller received compensation at the rate of $1,500 per month, and the gross sales in that year amounted to approximately $366,400 and the net sales to approximately $338,000. Consequently, even without considering the value of any of Mr. Miller's inventions which have been assigned to and used by the corporation royalty free, Mr. Miller's compensation cannot be said to be excessive. The fact that Mr. Miller during the period of time in question has assigned to the corporation, royalty free, two wire line wiper patents obtained in the United States, the Canadian patent on the open hole tool joint protector, the United States patent application on the open hole tool joint protector in respect to which two claims have been allowed, and all rights in respect to the remaining inventions would indicate that under no circumstances can it be said that Mr. Miller's compensation has been excessive. In fact on the basis of Mr. Dulin's letter of March 27, 1940, Mr. Miller has been underpaid.

"In considering the compensation paid to Mr. Ballagh, it is apparent from the evidence that Mr. Ballagh's services to the corporation have been of greater benefit to the corporation than those of Mr. Miller. If the corporation were required to pay a royalty of twenty-five cents on every protector installed by the hydraulic method (such as would be required under the Bettis cross-license agreement in the

event that the defendant corporation used the Bettis method), and similarly if the defendant corporation were required to pay reasonable royalties on lip protectors and pipe wipers, it would have paid out much more than has now been paid in the form of compensation. In addition the corporation would be a mere licensee and would not be the owner of the patents, a factor which is of great importance to the corporation and which places it in a position to make full use of the patent involved. Mr. Patterson, who was Mr. Miller's predecessor, had on various occasions engaged in inventive activities but had never given the corporation the benefit of the same [Tr. 163, 276-7]. The present policy of the corporation in taking assignments of any such inventions, royalty free, and of basing, in part, the compensation paid upon the proven value of such inventions has been determined upon by the board as the best business policy for the corporation to pursue, and it would appear that such an arrangement is much more advantageous to the corporation than any license agreement could be, whereby the corporation would not acquire title to the patent, and yet would be bound by an inflexible arrangement for many years to come.

"As to the law on the patents existing in this case and on those patents anticipated as the result of the inventions involved in this case, it is certain that prior to the assignments of such patents or patent applications, title to the patents or patent rights was in the individual defendants."

EXCERPTS FROM CASES CITED AT PAGES 68-69 OF BRIEF ON THE QUESTION OF AN IMPLIED CONTRACT REQUIRING A CORPORATION TO PAY THE REASONABLE VALUE OF SERVICES RENDERED BY ITS OFFICERS, AND ON THE QUANTUM MERUIT THEORY.

Fox v. Arctic Placer Min. & Mil. Co. (N. Y.), 128 N. E. 154 (Br. p. 68):

"It is well-settled rule that directors and officers of a corporation serve without compensation for performing the usual and ordinary duties of their offices, unless an express provision is made therefor either by statute, charter, by-laws, or agreement. The question to be considered here, therefore, is whether the services rendered were outside the official duties of the plaintiff, and, if this be true, the rule is qualified.

"The basis of a recovery for personal services must, of course, be a contract, and this must either be proven or implied. If the contract be not expressed, *it may be implied from the mere rendition and acceptance of the service.* Then the presumption is created that such services were to be compensated, because no one is expected to labor without hire. Barney v. Fuller, 133 N. Y. 605, 30 N. E. 1007." (Italics ours.)

Spalding v. Enid Cemetery Ass'n. (Okla.), 184 Pac. 579 (Br. p. 68):

"As to the questions of law involved, counsel for both parties agree that the general rule is correctly stated in Fields v. Victor Building & Loan Co., 175 Pac. 529, as follows:

"'A president and general manager of a corporation cannot maintain an action based on a *quantum*

meruit for past services rendered as president and manager. when no compensation for such services is provided in the charter or by-laws, and no compensation is fixed by any valid resolution passed prior to the rendition of such services, providing for compensation for such services.'

"But counsel for defendant contends that the case at bar is not governed by the general rule, but falls within one of the well-established exceptions thereto found stated in 2 Thompson on Corporations, §1736. Counsel for plaintiff do not notice this contention in their brief, apparently relying for success upon the authority of Fields v. Victor B. & L. Co., *supra.* So in its last analysis the real question is whether the case is governed by the general rule, or does it fall within one of the recognized exceptions thereto? We are of the opinion that the case falls within the exceptions mentioned by Mr. Thompson and the other authorities relied on by counsel for the defendant in his brief. Mr. Thompson, in the section of his work just referred to, says:

" 'There is a class of cases which, relaxing in some respects the rigid rule of the earlier cases, and establishing what may, perhaps, be called the modern doctrine of compensation, hold that the officers of a corporation may, under certain circumstances, recover compensation for their services within the line of their duties, on a *quantum meruit* or an implied promise to pay therefor; that where there is no prior express request, but where the services are rendered under such circumstances as to imply a promise, then the officer may recover. The presumption that the services were gratuitous *may be overcome by slight evidence.*' " (Italics ours.)

"Among the cases cited by the learned author in support of the text in Nat. L. & I. Co. v. Rockland, 36 C. C. A. 370, 94 Fed. 335, where he says (and we agree with him)—

" 'The rule was fully and admirably stated by a federal court thus: "A thoughtful and deliberate consideration of this entire question, and an extended consideration of the authorities upon it, has led to the conclusion that this is the true rule: Officers of a corporation, who are also directors, and who, without any agreement, express or implied, with the corporation or its owners, or their representatives, have voluntarily rendered their services, can recover no back pay or compensation therefor; and it is beyond the powers of the board of directors, after such services are rendered, to pay for them out of the funds of the corporation, or to create a debt of the corporation on account of them. But such officers, who have rendered their services under an agreement, either express or implied with the corporation, its owners or representatives, that they shall receive reasonable, but indefinite compensation therefor, may recover as much as their services are worth; and it is not beyond the powers of the board of directors to fix and pay reasonable salaries to them *after they have discharged the duties of their offices*."' (Italics ours.)

From *Waters v. American Finance Co.* (Md.), 62 Atl. 357 (Br. p. 68):

"But, although we so find as to the alleged contract set out in the account, we are of opinion that there was error in granting this prayer. There was evidence tending to show that the appellant did sell at least 2,500 of the 3,500 shares of stock to Mr. and Mrs. Center—included in the subscription we

have spoken of. It is further shown that the appellee actually had in hand at least $5,000 of the money of the Giroux Company for a stock sold Mrs. Center, and in a statement written on the back of a check of the American Finance Company, dated April 11, 1904, payable to the Giroux Company, it credited itself with the commissions on the sale of the 3,500 shares of stock. If then the appellant did sell part of that stock, as he claims he did, and the appellee has in hand the fruits of the labors of the appellant, it would seem to be just that he should receive such compensation as may be found to be reasonable for any services thus rendered by him outside of his duties as vice president or director. There is nothing in the record to show that the sale of the stock was a part of his duties in either of those capacities, and it certainly could not have been required of him to go to Boston for such purpose."

Fitzgerald & Mallory Const. Co. v. Fitzgerald, 137 U. S. 100, 34 L. Ed. 608 (Br. p. 69):

"The character of all these services placed them outside of official duties proper.

"The general rule is well stated by *Mr. Justice Morton* (since chief justice of Massachusetts) in *Pew v. First Nat. Bank,* 130 Mass. 391, 395; 'A bank or other corporation may be bound by an implied contract in the same manner as an individual may. But, in any case, the mere fact that valuable services are rendered for the benefit of a party does not make him liable upon an implied promise to pay for them. It often happens that persons render services for others which all parties understand to be gratuitous. Thus, directors of banks and of many other corporations usualy receive no compensation. In such cases, however valuable the services may be, the law

does not raise an implied contract to pay by the party who receives the benefit of them. To render such party liable as a debtor under an implied promise, it must be shown, not only that the services were valuable but also that they were rendered under such circumstances as to raise the fair presumption that the parties intended and understood that they were to be paid for; or, at least, that the circumstances were such that a reasonable man in the same situation with the person who receives and is benefited by them would and ought to understand that compensation was to be paid for them.' Tested by this rule, we think that the court fairly left it to the jury to determine whether Fitzgerald rendered services of such a character and under such circumstances that he was entitled to claim compensation therefor."

Gumaer v. Cripple Creek Tunnel, etc. Co. (Colo.), 90 Pac. 81 (Br. p. 69):

"The second contention of appellant is that the $8,000 note was made without consideration. and was practically a gift to defendant Wallace. Appellant contends that the evidence as to the alleged services for which the $8.000 was allowed falls far short of showing that they were outside of the line of his duty as an officer and director of the company. There is no evidence that the president or any of the members of the board of directors was bound to perform any duties in addition to those usually performed by like officers in similar corporations. Without attempting to enumerate the ordinary duties of such officers. it is sufficient to say that the services performed by defendant Wallace were largely in excess of those which he was bound to perform as an officer of the corporation. It appears from

the testimony that Wallace spent a great deal of time and rendered valuable services to the company; that he saved the company's entire property from being sold under execution and under decrees to satisfy miners' and mechanics' liens; that he undertook the placing of the stock of the company; that he assumed the entire supervision of the tunnel work and disbursement of the funds, the employment of men, and the making of contracts. His services differed from the other officers of the company, in that he devoted almost his entire time for a portion of each year to the financing and management of the corporation affairs. He was put to much expense in railroad and traveling expense. He gave of his stock to others and secured their assistance, including the 3,750 shares presented to plaintiff. Obviously, therefore, under the testimony, the services which the plaintiff performed were not those of a director or president, but outside thereof and similar to those of a general manager. Corinne Mill, Canal & Stock Co. v. Toponce, 152 U. S. 405, 14 Sup. Ct. 632, 38 L. Ed. 493. In Ruby Chief M. & M. Co. v. Prentice, 25 Colo. 4, 52 Pac. 210, it was said: 'Under the latter and better reasoned cases, for such services (that is, services performed by a director clearly outside of his duties as such director and in the nature of the duties of a general manager or superintendent) a recovery may be had either under an express or implied contract. * * * In Brown v. Silver Mines, 17 Colo. 421, 30 Pac. 66, 16 L. R. A. 426, there was no occasion to announce the rule that should govern in this jurisdiction, nor, as a matter of fact, was there any such ruling. In the absence of a controlling precedent of our own, it is a salutary general rule to follow the decision of the Supreme

Court of the United States. For services clearly outside the director's duties, as a director, we think there may be a recovery; as upon *quantum meruit,* under, and in accordance with, what, in Brown v. Silver Mines, *supra,* is denominated the "more liberal rule."' The testimony clearly showing that the duties performed by Wallace were in addition to those which he was required to perform as the president or a director of the corporation, he is entitled to compensation therefor, and the court erred in enjoining the collection of so much of the judgment as was based upon the $8,000 note."

Montana Tonopah Mining Co. v. Dunlap (C. C. A. 9th), 196 Fed. 612 (Br. p. 69):

"Notwithstanding the fact that there was no definite and valid exception to the charge of the court, we have nevertheless examined the charge, and find that it contains a full and fair statement of the law applicable to the case as presented by the evidence. It is in accordance with the decisions of the Supreme Court upon the subject, and with the great weight of authority in this country. In the case of Fitzgerald Construction Company v. Fitzgerald, 137 U. S. 98, 111, 11 Sup. Ct. 36, 41 (34 L. Ed. 608), the court approved the following statement of the general rule:

"'A bank or other corporation may be bound by an implied contract in the same manner as an individual may. But in any case, the mere fact that valuable services are rendered for the benefit of a party does not make him liable upon an implied promise to pay for them. It often happens that persons render services for others which all parties understand to be gratuitous. Thus directors of

banks and of many other corporations usually receive no compensation. In such cases, however valuable the services may be, the law does not raise an implied contract to pay by the party who receives the benefit of them. To render such a party liable as a debtor under an implied promise, it must be shown, not only that the services were valuable, but also that they were rendered under such circumstances as to raise the fair presumption that the parties intended and understood that they were to be paid for; or, at least, that the circumstances were such that a reasonable man, in the same situation with the person who receives and is benefited by them, would and ought to understand that compensation was to be paid for them.'

"In the case of National Loan & Investment Company v. Rockland Company, 94 Fed. 335, 338, 36 C. C. A. 370, 373, the Court of Appeals for the Eighth Circuit had before it the fundamental question here involved, and summed up its conclusions in respect to it as follows:

" 'A thoughtful and deliberate consideration of this entire question, and an extended consideration of the authorities upon it, has led to the conclusion that this is the true rule: Officers of a corporation, who are also directors, and who, without any agreement, express or implied, with the corporation or its owners, or their representatives, have voluntarily rendered their services, can recover no back pay or compensation therefor; and it is beyond the powers of the board of directors, after such services are rendered, to pay for them out of the funds of the corporation, or to create a debt of the corporation on account of them. Jones v. Morrison, 31 Minn. 140, 147, 16 N. W. 854; Blue v. Bank, 145 Ind. 518,

522, 43 N. E. 655; Doe v. Transportation Co. (C. C.) 78 Fed. 62, 67; Association v. Stonemetz, 29 Pa. 534; Railroad Co. v. Ketchum, 27 Conn. 170; Road Co. v. Branegan, 40 Ind. 361, 364. But such officers who have rendered their services under an agreement, either express or implied, with the corporation, its owners or representatives, that they shall receive reasonable, but indefinite, compensation therefor, may recover as much as their services are worth; and it is not beyond the powers of the board of directors to fix and pay reasonable salaries to them after they have discharged the duties of their offices. Missouri River Co. v. Richards, 8 Kan. 101; Rogers v. Railway Co., 22 Minn. 25, 27; Railroad Co. v. Tiernan, 37 Kan. 606, 15 Pac. 544, 553; Stewart v. Railroad Co. (C. C.), 41 Fed. 736, 739; Rosborough v. Canal Co., 22 Cal. 557, 562.'

"See, also, Corinne Mill, Canal & Stock Co. v. Topence, 152 U. S. 405, 14 Sup. Ct. 632, 38 L. Ed. 493; Clark & Marshall on Private Corporations, §671c, p. 2053; 2 Cook on Corporations (6th Ed.), §657, p. 1929 *et seq.*, and the numerous cases there cited."

Denman v. Richardson (C. C. A. 9th), 292 Fed. 19 (Br. p. 69):

"We find no error in the refusal to instruct the jury that the defendant while acting as trustee could not recover pay for past services, in the absence of some express provision therefor by statute, charter, or by-laws, or some agreement to that effect made and entered into before the services were rendered. The corporation was dissolved after having conducted its business for a period of about 19 years. It had offices at Tacoma, Wash., and branches in Alaska,

British Columbia, and Scotland. It owned ranches in Alberta. It had 5,000 head of cattle. It raised large crops of wheat. It owned and operated steamers and cold storage plants. *The president was not by the by-laws made the manager of the corporation.* The liquidation of the assets was a matter entirely distinct from the management of the corporation. There was evidence that the services rendered by the defendant were of a value much greater than the sum which was paid him, that the liquidation was very ably managed, that it was all done under the immediate direction of the defendant, and that it was wholly outside of the scope of his duties as fixed by the by-laws. In Bloom v. Bloom Codfish Co., 71 Wash. 41, 127 Pac. 596, the Supreme Court of Washington affirmed the general rule that where a president of a corporation renders services as a general manager with the consent of the other officers, he may recover on an implied contract for such services without any express contract therefor. In Fitzgerald Const. Co. v. Fitzgerald, 137 U. S. 98, 11 Sup. Ct. 36, 34 L. Ed. 608, the court held that while an officer of a corporation may recover compensation for performing the usual and ordinary duties of his office, only when there is an express agreement therefor, yet he may be entitled to compensation under an implied contract where he has performed services clearly outside his ordinary duties under circumstances which indicate that it was understood by the other officers of the corporation and by himself that his services were to be paid for. This court made application of the rule in Montana Tonopah Mining Co. v. Dunlap, 196 Fed. 612, 116 C. C. A. 286, holding that an officer or director of a corporation may recover reasonable compensation for services rendered for the corporation outside the

scope of his official duties, if the services were rendered under such circumstances as to raise the fair presumption that the parties intended and understood that they were to be paid for it. Among other cases so holding are National Loan & Investment Co. v. Rockland Co., 94 Fed. 335, 36 C. C. A. 370, and see 7 R. C. L. 465; 14a C. J. 137." (Italics ours.)

Zellerbach v. Allenberg, 99 Cal. 57, 33 Pac. 786 (Br. p. 69):

"It appears from the statement that it was shown at the trial 'that Allenberg had rendered various services other than those required of him as secretary, and had received the sum of $2,400 therefor,' and that the payment of this sum was authorized by a resolution passed by the board of directors of the company. The only evidence brought up in the record to show that the allowance and payment were improper is that of Mr. Zellerbach, in which he stated 'that in 1879 the trustees of the Altoona Quicksilver Mining Company voted Allenberg a compensation of $2,400 for services outside of his secretary's work, against which he, Zellerbach, protested as strongly as he could.'

"It was proper, if Allenberg performed extra services, that he be paid a reasonable and just compensation therefor, and that he did perform such services and received only a reasonable compensation for them *must be assumed in view of the action of the board.* Of course, he could not, as a member of the board, himself take part in passing the resolution to pay him the money, *and it does not appear that he or even E. L. Goldstein did take any part in passing it. There were five directors, and in the*

absence of anything to the contrary, it will be presumed that the resolution was authorized and was properly passed." (Italics ours.)

Appropriate excerpts from *Bassett v. Fairchild,* 132 Cal. 637, 52 L. R. A. 611, 64 Pac. 1082 (Br. p. 69) on the same point:

> "Immediately after the organization of the corporation, and in September, 1891, Fairchild was duly elected vice-president and general manager, and remained such during the time mentioned in the complaint. He immediately commenced to perform his duties as general manager, which duties were numerout and onerous, and occupied almost his entire time. The various kinds of work which he did as manager fully appear in the evidence, and need not be here given in detail; it is sufficient to say that his work included direction and supervision of the mining operations in the various leased mines; the supplies required; contracting for hauling rock from mines to cars; purchasing sacks for the rock; attending to shipping-receipts and collecting moneys; securing transportation facilities; chartering vessels for shipping rock to points on the northern Pacific coast; seeing that cars which came to San Francisco were properly loaded and delivered in proper shape to purchasers; looking after office management, and attending to all 'business of the corporation which came along from day to day.' Before his employment he had visited points as far north as Vancouver, British Columbia, in the interest of the use and sale of bituminous rock, and had become acquainted with public officials and others having control of street-paving, and was thus enabled to procure contracts with them for sale of the rock of the corporation. There is no doubt that his services were highly valuable, and

there is no doubt that they were of such a character as to preclude any reasonable supposition that they were to be gratuitous. *But there was no resolution of the board of directors and no express contract determining what compensation he should have for his services as manager, prior to November 9, 1892; and for this reason it is contended by respondents that he cannot legally have any compensation prior to that date.* Fairchild expected to receive compensation for his work as manager, the amount to depend somewhat upon the volume of business that would be developed and the testimony of Walrath, president, and Perine, treasurer of the corporation, shows that it was not expected by them or the other directors that he was to work gratuitously; Moreover, his work as manager was done with the knowledge of the directors, but there was no formal action taken on the subject until November 9, 1892." (Italics ours.)

And further on the lack of necessity of a formal allowance of compensation by the board of directors, pages 642-645:

"The by-laws provide that 'the compensation and terms of office of all officers of the corporation (other than directors) shall be fixed and determined by the board of directors.' *This language does not, on its face, mean that the compensation must be expressly and definitely agreed upon and settled before performance of the services;* but respondents contend that under the general law established by judicial decisions there can be no lawful allowance to an officer of a corporation for services, no matter what their character and value, where the amount of the compensation had not been fixed prior to the rendition of the

services. Many authorities on this subject have been cited on both sides, and they are to some extent conflicting. Most of those cited by respondents merely declare the rule that a 'director' *as such,* without some previous understanding, is not entitled to pay for services which are within the ordinary duties to be expected of him as director, although some of them, no doubt, apply the rule to other officers or agents who are also directors; but as to the last proposition the weight of authority and reason is the other way. (Italics ours.)

"As a general rule, when one person performs valuable services for another, whether the other be a corporation or a natural person, the law raises an implied promise to pay a reasonable compensation for the services, unless they are performed under circumstances which show an understanding that they were to be gratuitous. It frequently happens that one natural person performs valuable services for another natural person for which the former cannot recover, because circumstances show that they were rendered without any expectation of compensation. Now, it has been held that directors of corporations cannot, without previous express contract, receive compensation for such ordinary services as are usually rendered by directors without pay, for the common understanding, as declared by judicial decisions, is, that such services are presumed to be rendered gratuitously. But that presumption does not apply to those onerous services performed by officers and agents of a corporation, though they be also directors, for which compensation is usually demanded and allowed, and which could not reasonably be expected to be performed for nothing. The correct rule is stated by the United States Supreme Court in *Fitzgerald etc. Const.*

Co. v. Fitzgerald, 137 U. S. 98. In that case, Fitzgerald, who was a director of a corporation and its treasurer, acted as superintendent and general manager, and, as such, did valuable work 'not at all pertaining to his office as director,' and the question was, whether he was entitled to compensation for such work done before any compensation was fixed. The opinion of the court states that the trial court 'instructed the jury that, "if Fitzgerald, the plaintiff, acted as superintendent, treasurer, or general manager of said company, and transacted the usual business that devolves upon such officer of such a concern as that, with the knowledge and consent of the defendant" (during the time before compensation was fixed), there would be an implied agreement on the part of the defendant to pay what the services are reasonably worth, and afterwards repeated this instruction more in detail, confining it to services as manager.' The verdict was for Fitzgerald, and the judgment was affirmed. The court said: 'The general rule is well stated by Mr. Justice Morton (since chief justice of Massachusetts) in *Pew v. First Nat. Bank etc.,* 130 Mass. 391, 395: "A bank or other corporation may be bound by an implied contract in the same manner as an indiidual may. But, in any case, the mere fact that valuable services are rendered for the benefit of the party does not make him liable upon an implied promise to pay for them. It often happens that persons render services for others which all parties understand to be gratuitous. Thus directors of banks and of many other corporations usually receive no compensation. In such cases, however valuable the services may be, the law does not raise an implied contract to pay by the party who receives the benefit of them. To render such party liable as a debtor under an implied promise, it must

be shown not only that the services were valuable, but also that they were rendered under such circumstances as to raise the fair presumption that the parties intended and understood that they were to be paid for; or, at least, that the circumstances were such that a reasonable man, in the same situation with the party who receives and is benefited by them, *would and ought to understand that compensation was to be paid for them.*" Tested by this rule, we think that the court fairly left it to the jury to determine whether Fizgerald rendered services of such a character and under such circumstances that he was entitled to claim compensation therefor. *It could not properly have been held, as matter of law, that he was not so entitled.*' (Italics the Court's.)

"*Rogers v. Hastings etc. Ry. Co.*, 22 Minn. 25, is a case directly in point. It is stronger in support of the proposition above stated than the case at bar, because the charter of the corporation in that case provided that the board of directors should appoint the officers 'and fix their compensation for the services *to be rendered.*' Rogers was a director, and was appointed secretary of the corporation, and also acted as its land commissioner and attorney, and sued for the value of services rendered in such capacities. There had been no compensation fixed, nor any contract made, before the services were rendered; and it was contended there, as here, that no compensation could be recovered for past services. But it was held otherwise. The court said, among other things, as follows: 'The evidence showed that the plaintiff. while acting as land commissioner, was a member of the board of directors. If his services as land commissioner had been performed by him simply *as a director,* it might be that he could not recover for the same, since, in the absence of a special agreement for

compensation, he would, according to many authorities, be presumed to have acted gratuitously. But the duties and labors of a land commissioner of a land-grant railroad company do not necessarily nor presumptively pertain to a director as such. Indeed, it would be unreasonable to suppose that duties so onerous would be undertaken by one acting simply as a director without pay. For such extraordinary services, outside of and beyond his duties as director, a party may certainly recover, notwithstanding his directorship, for the reason that, even if he performs the duties of director gratuitously, these services are not a part of those duties.' (Citing cases.)" (Italics the Court's.)

Appropriate excerpts from *King v. Grass Valley Gold Mines Co.,* 205 Cal. 698, 272 Pac. 290 (Br. p. 69):

> "In short, we see no reason here for withholding application of the rule announced in the case of *Bassett v. Fairchild,* 132 Cal. 637 (52 L. R. A. 611, 64 Pac. 1082), to the effect that the presumption that certain corporate officers render their services gratuitously in the absence of previous express contract, does not apply to onerous services, which could not reasonably be expected to be performed for nothing, although no compensation therefor is previously fixed; and in such cases there is an implied agreement to pay what the services are reasonably worth."

Excerpt from *San Leandro Canning Co. Inc. v. Perillo,* 84 Cal. App. 635 (Br. p. 69):

> "As to the two director-defendants, it is alleged that neither of them had a prior contract or agreement with said corporation whereby they, or either

of them, was to be paid a commission for making sales of the corporate stock. As we understand the argument of the appellant it is to the effect that the claims for compensation of the two director-defendants were, therefore, *ultra vires* the corporation and could not legally be paid. If this were an action by said directors to recover compensation for the value of their services so rendered, it will be conceded at once that a prior authorization would be of importance. But that rule is not without limitation. In *Bassett v. Fairchild,* 132 Cal. 637, 643 (52 L. R. A. 611, 64 Pac. 1082), the court said: 'Now, it has been held that directors of corporations cannot, without previous express contract, receive compensation for such ordinary services as are usually rendered by directors without pay, for the common understanding, as declared by judicial decisions is, that such services are presumed to be rendered gratuitously. But that presumption does not apply to those onerous services performed by officers and agents of a corporation, though they be also directors, for which compensation is usually demanded and allowed, and which could not reasonably be expected to be performed for nothing.' (See, also, *Hughes v. Pacific Wharf etc. Co.,* 188 Cal. 210, 216 (205 Pac. 105).) But we are running afield. *This is not an action by a director to recover compensation. The complaint alleges that the directors have already been paid. This is an action to recover back those payments.* Counsel do not cite any authorities, and we know of none, to the effect that, in the absence of allegations of fraud, the mere averment that without a prior authorization the payment to a director for services admittedly rendered would be either a void or a voidable transaction." (Italics ours.)

Quotations From Cases Cited by Appellant at Page 40 of Its Brief.

Jones v. Foster (C. C. A. 4th), 70 Fed. (2d) 200 (Br. p. 70):

"In instructing the jury to disallow this claim the district judge acted on the view that the services performed were clearly not outside the scope of the duties pertaining to the defendant's office as president of the corporation in accordance with the By-Laws, especially when considered in the light of the original agreement or understanding between the parties and bearing in mind the defendant's personal interest as majority stockholder of the corporation and relation of creditor by virtue of the substantial loans to the corporation for working capital. In our opinion the view so taken is reasonable and sound. In the absence of an express agreement by the corporation to pay for services *within the scope of the officer's duties* there could be no valid claim for compensation. Baltimore Co. v. Dinning, 141 Md. 318, 321, 118 A. 801." (Italics ours.)

From syllabus in *Pindell v. Conlon Corp.* (Ill.), 24 N. E. (2d) 882 (Br. p. 71):

"A director was not entitled to compensation for allegedly obtaining a manufacturing contract for corporation, where alleged oral agreement with president of corporation provided for the securing of a purchaser for corporation and not a manufacturing contract, and director, in absence of a by-law or resolution of board of directors, was not entitled to compensation for services rendered *within the scope of his duties as a director*." (Italics ours.)

From syllabus in *Larkin v. Enright,* 37 N. E. (2d) 905 (Br. p. 71):

"*Corporations*

"In suit to restrain defendant from voting two shares of stock standing in his name on books of corporation, evidence disclosed that plaintiff delivered stock to defendant to hold for a limited use and to be returned by request, and that plaintiff was the legal owner of the two shares involved.

"*Corporations*

"Where defendant was director and secretary of corporation and an employee receiving $75 weekly when he obtained reduction of corporation's mortgage indebtedness and an extension of the mortgage, he was not entitled to extra compensation in the absence of a by-law or resolution authorizing payment thereof.

"*Corporations*

"Contention that person who was president of corporation promised employee, who was a director and secretary, 'at some later date to make it all right with him' for his services in obtaining reduction and extension of corporation's mortgage, was too vague and uncertain to form basis of a contractual obligation.

"*Corporations*

"Where president of corporation agreed that one who was employee and stockholder should hold two shares of stock belonging to president for limited use and return it upon request, failure to return stock justified court in restraining holder from using such stock to gain control of corporate affairs."

In re Dr. Voorhees Awning Hood Co. (D. C. Pa.), 187 Fed. 611 (Br. p. 71):

> "The other matters were correctly disposed of except one, and require no extended consideration. The claimant, being president of the company, had no right to a commission on sales either of stock or material, except as there was a distinct agreement to that effect, which has not been shown. Althouse v. Cobaugh Colliery Co., 227 Pa. 580, 76 Atl. 316. It affords no basis for such a claim that they were allowed to others. Nor is it of any consequence that $138 was actually paid him by the company on this account. Just how this came about does not appear. The directors may have felt that he ought to be remunerated to that extent for his services in this connection without thereby establishing his rights as a legal claim to the remaining $62 contended for."

EXCERPTS FROM CASES CITED ON THE QUESTION OF THE PROPRIETY INTEREST OF THE INDIVIDUAL DEFENDANTS IN THEIR INVENTIONS AND DEVICES, AS WELL AS SHOP RIGHTS THEREIN, IN THE ABSENCE OF COMPENSATION THEREFOR AND ASSIGNMENTS THEREOF.

United States v. Dubilier Corp., 289 U. S. 178, 77 L. Ed. 1114 (Br. p. 72):

> "A patent is property and title to it can pass only by assignment. If not yet issued an agreement to assign when issued, if valid as a contract, will be specifically enforced. The respective rights and obligations of employer and employee, touching an invention conceived by the latter, spring from the contract of employment.
>
> "One employed to make an invention, who succeeds, during his term of service in accomplishing that

task, is bound to assign to his employer any patent obtained. The reason is that he has only produced that which he was employed to invent. His invention is the precise subject of the contract of employment. A term of the agreement necessarily is that what he is paid to produce belongs to his paymaster. Standard Parts Co. v. Peck, 264 U. S. 52, 68 L. ed. 560, 44 S. Ct. 239, 32 A. L. R. 1033. On the other hand, if the employment be general, albeit it covers a field of labor and effort in the performance of which the employee conceived the invention for which he obtained a patent, the contract is not so broadly construed as to require an assignment of the patent. Hapgood v. Hewitt, 119 U. S. 226, 30 L. ed. 369, 7 S. Ct. 193; Dalzell v. Dueber Watch Case Mfg. Co., 149 U. S. 315, 37 L. ed. 749, 13 S. Ct. 886. In the latter case it was said:

"'But a manufacturing corporation, which has employed a skilled workman, for a stated compensation, to take charge of its works, and to devote his time and services to devising and making improvements in articles there manufactured, is not entitled to a conveyance of patents obtained for inventions made by him while so employed, in the absence of express agreement to that effect.'

"The reluctance of courts to imply or infer an agreement by the employee to assign his patent is due to a recognition of the peculiar nature of the act of invention, which consists neither in finding out the laws of nature, nor in fruitful research as to the operation of natural laws, but in discovering how those laws may be utilized or applied for some beneficial purpose, by a process, a device or a machine. It is the result of an inventive act, the birth of an idea and its reduction to practice; the product of

original thought; a concept demonstrated to be true by practical application or embodiment in tangible form. Clark Thread Co. v. Williamantic Linen Co., 140 U. S. 481, 489, 35 L. ed. 521, 525, 11 S. Ct. 846; T. H. Symington Co. v. National Castings Co., 250 U. S. 383, 386, 63 L. ed. 1045, 1049, 39 S. Ct. 542; Pyrene Mfg. Co. v. Boyce (C. C. A. 3d) 292 Fed. 480, 481.

"Though the mental concept is embodied or realized in a mechanism or a physical or chemical aggregate, the embodiment is not the invention and is not the subject of a patent. This distinction between the idea and its application in practice is the basis of the rule that employment merely to design or to construct or to devise methods of manufacture is not the same as employment to invent. Recognition of the nature of the act of invention also defines the limits of the so-called shop right, which shortly stated, is that where a servant, during his hours of employment, working with his master's materials and appliances, conceives and perfects an invention for which he obtains a patent, he must accord his master a non-exclusive right to practice the invention. McClurg v. Kingsland, 1 How. 202, 11 L. ed. 102; Solomons v. United States, 137 U. S. 342, 34 L. ed. 667, 11 S. Ct. 88; Lane & Co. v. Locke, 150 U. S. 193, 37 L. ed. 1049, 14 S. Ct. 78. This is an application of equitable principles. Since the servant uses his master's time, facilities and materials to attain a concrete result, the latter is in equity entitled to use that which embodies his own property and to duplicate it as often as he may find occasion to employ similar appliances in his business. But the employer in such a case has no equity to demand a conveyance of the invention, which is the original conception of the em-

ployee alone, in which the employer had no part. This remains the property of him who conceived it, together with the right conferred by the patent, to exclude all others than the employer from the accruing benefits. These principles are settled as respects private employment."

On the same point from *Deane v. Hodge* (Minn.), 27 N. W. 917 (Br. p. 72):

"Where the evidence fails to disclose an express agreement or understanding, the law may imply a contract from the circumstances or the acts of the parties; and where there is nothing from which a contrary intention or understanding is to be inferred, it is a just and reasonable presumption that he who has received the benefit of the services or property of another impliedly undertakes to make compensation therefor. 'Implied contracts are such as reason and justice dictate, and which, therefore, the law presumes that every man has contracted to perform.' 3 Bl. Comm. *158; 2 Kent, Comm. *450; Bouv. Law Dict. 'Obligations, Implied;' 2 Greenl. Ev. §108. A patent is a mere monopoly or exclusive right to an invention, not existing at the common law, but by special grant from the government. The defendant therefore contends that, unless there is an express contract defining the terms of use by a licensee, the patentee is confined to the remedy provided by the patent law for an infringement, by an action on the case for damages, and that there can be no such thing as an implied license for compensation.

"There is very little authority on the subject, as the question of implied license has usually arisen in actions for infringement, and as such is for a

tortious use or piracy, and the existence of a license, express or implied, is always a sufficient defense. But an action upon a contract, express or implied, for compensation for the use of a patented invention, or for license fees, is not one arising under the patent laws; and, notwithstanding the nature of the subject, common-law principles are applicable, as in other cases. Thus, in *McClurg v. Kingsland, supra,* the court held that, if the facts were as testified, 'they would justify the presumption of a license or special privilege or grant to the defendants to use the invention, and show such a consideration as would support an express license or grant, or *call for a presumption of one, to meet the justice of the case,* by exempting them from liability, having equal effect with a license, and giving the defendants *a right to the continued* use of the invention.' Here is recognized the principle that, from the circumstances and to meet the justice of the case, a license or grant for a continued use of the invention would be implied. The right to use and profit by a patented invention may, then, be the subject of contract; and if the evidence of an express contract is wanting, it may be implied, as in other cases, and for the same reasons; and if *assumpsit* will lie upon express contract to recover reasonable license fees or compensation, it may also be maintained upon implied contract, though, from the nature of the subject, and the circumstances of any particular case, the question may be involved and difficult of solution. See Walk. Pat., §312; *DeWitt v. Elmira Manuf'g Co.*, 66 N. Y. 461. In *McKeever v. U. S.,* 14 Ct. Cl. 396, it was held that where the patentee had allowed the defendant to proceed in the manufacture and use of a patented invention or article 'without the formality of an express license, or the precaution

of an express consideration, the omission did not change the character of the transaction, for the law supplies, by implication, a price in giving what the license was reasonably worth.' The case was well considered, and was afterwards affirmed by the supreme court of the United States. Walk. Pat. §391.

"Recurring again to the question of the relationship of the plaintiff to the defendant as president or director at the time, as affecting his cause of action, it was held in *Rogers v. Railroad,* 22 Minn. 25, that a defendant corporation, or which the plaintiff was a director, might be held liable upon an implied *assumpsit* to pay the reasonable value of services rendered for defendant outside of his duties as director. He could not, as director, aid by his vote in fixing the amount of such compensation, for in that case there would be a conflict of interests inconsistent with his official duty. *Jones v. Morrison,* 31 Min. 148; S. C. 16 N. W. Rep. 854. But the rule is not, as we understand it, to be carried so far as to prevent the corporation from availing itself of the services or property of an officer of the company, 'if necessary for its convenience or profits, as in the case of other persons, under circumstances implying a contract to pay a reasonable compensation therefor.' *Rider v. Rubber Co.,* 5 Bosw. 97. All such dealings are, of course, looked upon with jealousy by the courts, and the fact of such official relationship, and the interest of the officer in the affairs and property of the corporation, would figure prominently in determining the question of fact whether or not a contract for a compensation is to be implied. *Gardner v. Butler,* 30 N. J. Eq. 703.

"Upon the directors was imposed the duty and authority, which was exercised by them, of determining the character and number of the machines

to be manufactured. The improvement was appropriated and used by them, or under their direction, on behalf of the company; and the continued acquiescence of the corporation for several years sufficiently indicate its approval. *Rider v. Rubber Co.,* 5 Bosw. 96." (Italics the Court's.)

Heywood-Wakefield Co. v. Small (C. C. A. 1st), 87 Fed. (2d) 716 (Br. p. 72):

"The defendant has a large factory in which it manufactures, *inter alia*, car seats for trolley cars and railroad coaches. It first employed the plaintiff in the fall of 1927 as a draftsman. This employment continued until March, 1928, when Small was promoted and made a 'checker.' It was while employed as a checker in July, August, and September, 1928, that Small invented the car seat base for which the patent in suit was issued.

"The defendant contends that the plaintiff was employed to invent improvements in its line of goods and that the results of his efforts at invention belong to his employer. Houghton v. United States (C. C. A.) 23 F. (2d) 386, 390; United States v. Dubilier Condenser Corp., 289 U. S. 178, 53 S. Ct. 554, 77 L. Ed. 1114, 85 A. L. R. 1488. The plaintiff says that his employment was not of that character. There was some conflict of testimony as to what duties were involved in plaintiff's work as 'checker.' The defendant's contention was that if the plaintiff 'saw, as he checked through the work, that improvements could be made on it, * * * he could offer these suggestions and have changes made in the drawings' that such duties 'went with the position of checking.' The plaintiff testified that his duties were 'to check every part of the car seat, and all parts of the car seat,—reed furniture shop, machine shop,

wood shop, upholstery shop, cutting room, and paint shop. My work was entirely on car seats. * * * It was my job to see that the goods were made according to the orders.' The plaintiff's immediate superior, a Mr. Eichel, testified that: 'The duties of checker were to look over the products of manufacture whenever it was requested from the shop, the foreman or the superintendent.' We generally went down, looked them over and passed on them. And then before the article went through to another department that was going to use it, they would request a check on it. The checker would change the orders, would check the drawings in the drafting room and check the work in the shop from those drawings.

"Eichel further testified that he did not recall ever having given the plaintiff definite orders to design a rotating car seat base; and no such instructions appear to have been given to the plaintiff by anybody else. Nor does it appear that the plaintiff was ever assigned to the work of inventing improvements on the company's products.

"In finding that 'originating new developments was not part of the plaintiff's duties in this capacity (as checker)' it certainly cannot be said that the District Judge was clearly in error. It follows that the defendant was not entitled to an assignment of the patent."

On the question of "shop rights" the Court says:

"On the question of whether the defendant was entitled to a 'shop right' either upon the basis of a contract on the ground that the work of invention was on the defendant's time and at its expense, or on the ground of estoppel, that he saw his inven-

tion being used by the defendant without protest on his part, none of the cases cited supports the defendant's contention.

"The cases of McClurg v. Kingsland, 1 How. 202, 11 L. Ed. 102; Solomons v. United States, 137 U. S. 342, 346, 11 S. Ct. 88, 34 L. Ed. 667; Lane & Bodley Co. v. Locke, 150 U. S. 193, 14 S. Ct. 78, 37 L. Ed. 1049; Keyes v. Eureka Mining Co., 158 U. S. 150, 15 S. Ct. 772, 39 L. Ed. 929; Gill v. United States, 160 U. S. 426, 16 S. Ct. 322, 40 L. Ed. 480, all differ widely from the facts in this case. In these cases either the plaintiff made the invention on his employer's time and at his employer's expense and it was a part of his duty to improve the methods used by his employer, or he stood by for a long period and permitted his employer to use his invention without protest before making any claim.

"Nor do we think the case of John M. Burton v. Burton Stock-Car Co., 171 Mass. 437, 50 N. E. 1029, has any bearing on the issues in this case. In that case there was an assignment of an invention with the stipulation that the plaintiff reserved the right to royalties in the future and was assured by the defendant that that would be adjusted later. The court said, at page 440 of 171 Mass. 50 N. E. 1029, 1030:

" 'There was no evidence, so far as appears, that the plaintiff agreed to license the use of his improvements gratuitously and in the absence of such an agreement an implied promise to pay might be inferred from the above facts. Walk. Pat. (2d Ed.) §312.' "

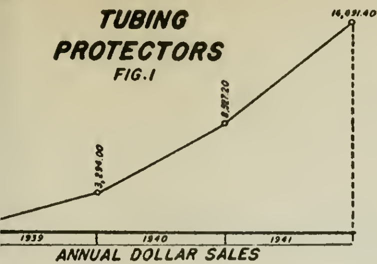
THE FOLLOWING ARE EXCERPTS FROM CASES CITED ON PAGES 76-77 OF THE BRIEF UNDER THE HEADING OF "RATIFICATION".

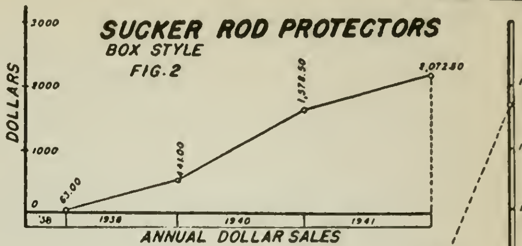
Middleton v. Arastraville Mining Co., 146 Cal. 219 (Br. p. 76):

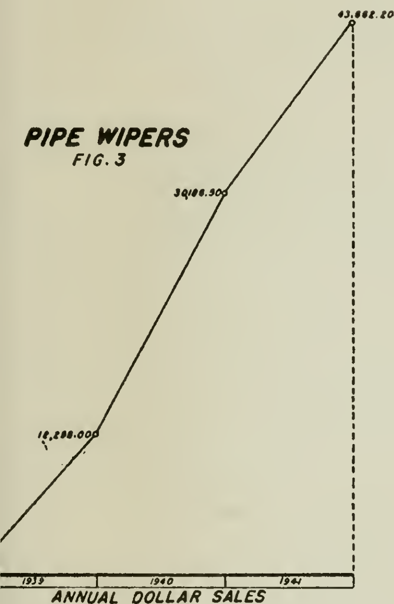
"The suggestion in the appellants' brief that by reason of his interest the plaitniff is disqualified from voting in favor of ratifying the act of the directors is without merit. The stockholders of a corporation do not hold a fiduciary relation to each other by which one is precluded from voting at a stockholders' meeting upon any question in which he has an individual interest adverse to any of the other stockholders." (P. 224.)

Klein v. Independent Brew. Co. (Ill.), 83 N. E. 434 (Br. p. 77):

"By his conduct subsequent to the meeting of November, 1901, *in participating in the election and re-election of the same officers year after year* and fixing their salaries, including a salary to himself, as director, of $300 per year, he is estopped from now asking an accounting on account of the salaries paid after said year 1901. Brown v. De Young, 167 Ill. 549, 47 N. E. 863; Rosehill Cemetery Co. v. Dempster, 223 Ill. 567, 79 N. E. 276; Cook on Corporations, §646. Furthermore, there is not a word of proof that the services of the officers of the corporation were not worth the salaries paid to them." (P. 442.) (Italics ours.)







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DOLLARS

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GROSS
SALES
TO
JUNE 1-1942.
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GRAPHIC CHARTS INDICATING
THE YEAR BY YEAR INCREASE IN DOLLAR SALES
OF
ROYALTY-FREE INVENTIONS
OF J. C. BALLAGH
OTHER THAN THE INVENTIONS
OF THE LIP PROTECTOR AND HYDRAULIC APPLICATOR